Supreme Court, U.S.
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No. _____

In The

Supreme Court of the United States

UNITED STATES OF AMERICA, ex rel. AMERICAN TEXTILE MANUFACTURERS INSTITUTE, INC.,

Petitioner,

v.

THE LIMITED, INC., et al.,
TARRANT APPAREL GROUP, et al.,

Respondents.

On Petition For A Writ Of Certiorari To The United States Court Of Appeals For The Sixth Circuit

PETITION FOR WRIT OF CERTIORARI

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QUESTIONS PRESENTED

The False Claims Act ("FCA") imposes liability on any person who makes a false statement to conceal an "obligation to pay or transmit money or property to the Government." 31 U.S.C. § 3729(a)(7). ATMI alleges that Defendants filed false statements to conceal unconditional obligations arising because of their unlawful importation of garments produced in the People's Republic of China but falsely labeled as and declared to be products of Hong Kong or Macau. The court of appeals held that the term *obligation* did not include obligations that a government official has discretion not to enforce. The district judge failed to disclose to Plaintiff's counsel that, less than two months previously, he had been represented by partners in the Defendants' law firm in a state criminal matter. The questions on which review is sought are:

1. Whether the court of appeals erred in holding that the "obligation" section of the False Claims Act does not apply to a defendant that owes money to the United States, and makes false filings and statements to conceal, avoid or decrease that obligation, if a government official would have discretion not to enforce the obligation.

2. Whether the court of appeals had an obligation to review the district judge's failure to disclose a serious and arguably disqualifying conflict of interest and failure to vacate his judgment after the conflict was revealed.

PARTIES TO THE PROCEEDING BELOW

Petitioners:

United States of America, ex rel. American Textile Manufacturers Institute, Inc.

Respondents:

The Limited, Inc.; The Limited London-Paris-New York, Inc.; Limited Too, Inc.; Intimate Brands, Inc.; Victoria's Secret Stores, Inc.; Victoria's Secret Catalogue, Inc.; Cacique, Inc.; Mast Industries, Inc.; Express, Inc.; Lerner New York, Inc.; Lane Bryant, Inc.; Henri Bendel, Inc.; Structure, Inc.; Abercrombie & Fitch, Inc. (collectively referred to as "the Limited Defendants"); Tarrant Apparel Group, d/b/a Fashion Resource, Inc.; Gerard Guez; and Todd Kay.

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The opinion of the United States Court of Appeals for the Sixth Circuit is published at 190 F.3d 729 and appended at App. 1. The opinion of Judge Holschuh of the United States District Court for the Southern District of Ohio dismissing the amended complaint is unpublished and is appended at App. 30. The opinion of Judge Holschuh denying Relator's motion to disqualify and vacate is unpublished and is appended at App. 74. The opinion of Judge Beckwith of the same district court denying ATMI's motion to vacate or to alter or amend the judgment is published at 179 F.R.D. 541 and is appended at App. 89.

JURISDICTION AND VENUE

The decision of the Sixth Circuit was entered on September 14, 1999. Rehearing and rehearing *en banc* were both denied on November 2, 1999. This Court has jurisdiction pursuant to 28 U.S.C. § 1254(1).

STATUTES AND REGULATIONS INVOLVED

The following statutes and regulations are involved in this case. Due to the length of the cited provisions, the pertinent text thereof is set out in the appendix hereto.

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STATEMENT OF THE CASE

A. Summary

The *qui tam* provisions of the False Claims Act ("FCA"), 31 U.S.C. §§ 3729 *et seq.*, permit private parties to bring suit in federal court to recover treble damages and penalties for the United States on account of, *inter alia*, the making of false records or statements to conceal, avoid, or decrease any "obligation" to pay money or transmit property to the United States. 31 U.S.C. § 3729(a)(7) (App. 114-116). Petitioner American Textile Manufacturers Institute, Inc. ("ATMI") brought this case under Section 3729(a)(7) against The Limited, Inc. and certain related companies, and Tarrant Apparel Group and two of its principal shareholders ("Defendants"). ATMI alleged that Defendants engaged in a practice of trade in which articles of apparel produced in the People's Republic of China were transshipped through Hong Kong or Macau, mislabeled as originating in those countries, and then unlawfully imported into the United

States. ATMI asserted that as a result of these acts Defendants had incurred unconditional obligations to pay duties and penalties to the United States and that *after* these obligations arose Defendants concealed the obligations by filing false records and statements with the U.S. Customs Service, triggering liability under Section 3729(a)(7). The district court dismissed the complaint for failure to state a claim, and the court of appeals affirmed.

B. Regulation of Imports and the Defendants' Conduct

The United States has entered into various international agreements that limit the quantities of products allowed to be imported from certain countries. In particular, a bilateral U.S.-China agreement imposes a quota on the amount of wearing apparel that may be imported into the U.S. from China. Because the cost of production in China is low, there is an economic incentive to import Chinese-made garments, but any importer's ability to do so lawfully is limited by this quota. The transshipment of garments from China to avoid quota limitations is a major problem. The United States Customs Service has estimated that the value of Chinese-made garments declared to be the products of other countries ranged between 6.4 and 10.7 billion dollars in 1992. *Unraveling The Mystery: Following the Thread of PRC Apparel Imports,* United States Customs Service, December 1994, at 1.

ATMI's amended complaint (which was dismissed and for present purposes must be taken as true) alleged that Defendants, which are clothing merchants, contrived to import Chinese-made garments in excess of the quota.

Specifically, they imported garments that had been manufactured in China but had been falsely marked "Made in Hong Kong" or "Made in Macau" and were accompanied by documentation declaring that they were products of Hong Kong or Macau. Moreover, because the garments were subject to quota restraints, visas issued by the real country of origin were required before they could be lawfully admitted into the commerce of the United States; the Defendants, however, improperly used visas from Hong Kong or Macau for this Chinese-made merchandise.

ATMI's amended complaint further alleged that these acts gave rise to several distinct obligations to pay money to the United States. Specifically, it alleged that Defendants are obligated (1) to pay a duty, which became due upon importation, equal to 10% of the value of all articles marked with an erroneous country of origin, *see* 19 U.S.C. § 1304(f) (now § 1304(h) (App. 134-135)); (2) to pay contractual liquidated damages to the United States, equal to the value of the merchandise, for breach of conditions set forth in their Customs bonds, *see* 19 C.F.R. §§ 113.62(k)(1) (App. 129-132) and 141.113 (App. 132-133); (3) to forfeit the improperly imported merchandise or cash equal to its value, *see* 18 U.S.C. § 545 (App. 125-126); (4) to pay civil money penalties equal to the value of the merchandise for aiding the unlawful importation of merchandise, *see* 19 U.S.C. § 1595a(b) (App. 126-127); (5) to pay civil money penalties not to exceed the domestic value of the merchandise for violating Customs laws, *see* 19 U.S.C. § 1592 (App. 127-129); and (6) to pay civil money penalties under the Textile Fiber Products Identification Act, 15 U.S.C. §§ 70 *et seq.* (App. 138-140), and the Federal Trade

Commission Act, 15 U.S.C. § 45(m) (App. 135-137), for unfair methods of competition or unfair and deceptive acts or practices consisting of the importation of misbranded textile products.

The statutory obligation to pay the ten percent marking duty springs into being when merchandise is imported with incorrect country of origin marking. That obligation may be extinguished if the marking is corrected or the merchandise is re-exported or destroyed. ATMI alleges that the Defendants never extinguished the obligation to pay marking duties by correcting the erroneous markings or by re-exporting or destroying this merchandise. Amended Complaint at ¶ 185 (App. 206-207).

The obligation to pay liquidated damages under the Customs bond is contractual. The conditions of the Customs bond are set out in the Customs Regulations at 19 C.F.R. § 113.62 (App. 129-132). Those conditions include the requirement that an importer redeliver into Customs' custody merchandise that is not properly marked or otherwise fails to comply with the laws or regulations governing admission into the United States. 19 C.F.R. § 113.62(d) (App. 129-132). The right of the United States to liquidated damages under 19 C.F.R. § 113.62(k)(1) (App. 129-132) and 141.113 (App. 132-133) is based upon its contract (bond) with the importer.

The obligations imposed by items 3, 4, and 5 are civil forfeitures and penalties that are normally assessed in the alternative by the Customs Service. Penalties and forfeitures are remedial and have traditionally been justified as a form of liquidated damages to make the government

whole on account of its loss incurred by reason of the violation of its international trade policy. *One Lot Emerald Cut Stones and One Ring v. United States*, 409 U.S. 232, 237 (1972); *United States v. Valley Steel Products Co.*, 14 C.I.T. 14, 17, 729 F. Supp. 1356, 1359-60 (1990).

ATMI's complaint further alleged that Defendants concealed these obligations by making false filings and statements *after* the unlawful importations which had given rise to these monetary obligations had taken place. The Amended Complaint is quite specific in alleging that each of these obligations arose at the time of importation and existed separate and apart from the false statements made to conceal these obligations. Amended Complaint at ¶¶ 147-193 (App. 198-209).

C. The False Claims Act

Qui tam statutes, providing for civil actions by knowledgeable private citizens to recover debts and other obligations owed to the sovereign, "have been in existence for hundreds of years in England, and in this country ever since the foundation of our government." *Marvin v. Trout*, 199 U.S. 212, 225 (1905); *see also United States ex rel. Marcus v. Hess*, 317 U.S. 537, 541 n.4 (1943), *citing Adams, qui tam, v. Woods*, 6 U.S. (2 Cranch) 336 (1805), as an early example of the use of *qui tam* statutes to recover civil penalties and forfeitures. Indeed, the availability of *qui tam* suits was once so commonplace that informers' statutes authorizing a moiety were assumed to include an implied right to file *qui tam* actions unless that right was specifically withheld. *Marcus v. Hess*, 317 U.S. at 541 n.4.

The First Congress enacted a number of *qui tam* provisions, several of them relating to recovery of sums owed under the Customs laws.[1] The use of such provisions as well as informer statutes to reward those who expose Customs fraud continues to the present.[2] This

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[1] *See United States ex rel. Stillwell v. Hughes Helicopters, Inc.*, 714 F. Supp. 1084, 1086 (C.D. Cal. 1989) (*citing* Act of July 31, 1789, ch. 5 sections 29, 38, 1 Stat. 29, 44-45, 48 (import duties); Act of Sept. 1, 1789, ch. 11 section 21, 1 Stat. 55, 60 (vessel registration); Act of March 1, 1790, ch. 2 sections 3, 6, 1 Stat. 101, 102-03 (census); Act of May 31, 1790, ch. 15 section 2, 1 Stat. 124, 124-25 (copyright infringement); Act of July 5, 1790, ch. 25 section 1, 1 Stat. 129 (census); Act of July 5, 1790, ch. 25 section 1, 4, 1 Stat. 131, 133 (seamen regulations); Act of July 22, 1790, ch. 33 section 3, 1 Stat. 137, 137-38 (regulation of Indian trade); Act of Aug. 4, 1790, ch. 35 sections 55, 69, 1 Stat. 145, 173, 177 (import duties); Act of Feb. 25, 1791, ch. 10 sections 8, 9, 1 Stat. 191, 195-96 (regulation of Bank of United States); Act of Mar. 3, 1791, ch. 15 section 44, 1 Stat. 199, 209 (liquor duties)).

[2] In addition to the statutes cited in n.1, *supra*, *see* Act of March 2, 1799, ch. 22 section 91, 1 Stat. 627, 697 (providing informer with one-half of all penalties, fines and forfeitures recovered); Act of March 3, 1823, ch. 58 section 5, 3 Stat. 781, 182 (amending the Act of March 2, 1799 and reaffirming the same informer provision); Act of March 1, 1823, ch. 21 section 35, 3 Stat. 729, 739 (amending the Act of March 2, 1799 and reaffirming the same informer provision); Act of July 18, 1866, ch. 201 section 31, 14 Stat. 178, 186 (amending the Act of March 2, 1799 and reaffirming the same informer provision); Act of March 2, 1867, ch. 188 section 1, 14 Stat. 546-47 (providing informant with one-fourth of the proceeds of fines, penalties, and forfeitures recovered); Act of June 22, 1874, ch. 391 section 4, 18 Stat. 186-87 (providing informer with up to $5,000 of any duties, fines, penalties or forfeitures recovered); Act of September 21, 1922, ch. 356 Title IV, § 619, 42 Stat. 988 (providing informant with 25% of any duties, fines, penalties or forfeitures recovered, not to exceed $50,000); Tariff Act of 1930,

Court recently noted that "suits for the payment of monetary [customs] forfeitures were viewed no differently than suits for the customs duties themselves." *United States v. Bajakajian*, 524 U.S. 321, ___, 118 S.Ct. 2028, 2040 n.18 (1998), *citing Stockwell v. United States*, 80 U.S. 531, 542 (1871) (suits to recover customs duties or forfeitures actionable in action of debt at common law because "the sum owing is capable of being definitely ascertained").

The statute under which this case was brought, the False Claims Act, was enacted in 1863 to address fraud against the federal government in connection with procurement of military supplies for the Civil War. Act of March 2, 1863, ch. 67 § 1, 12 Stat. 696; *Rainwater v. United States*, 356 U.S. 590, 592 (1958). Until 1986, the FCA applied clearly only to false claims for payments *by* the United States. There was a conflict in the case law prior to 1986 as to whether the FCA also applied to concealment of obligations owed *to* the United States. Congress resolved this conflict in 1986 by adding Section 3729(a)(7), which imposes liability on any person who "knowingly makes, uses or causes to be made or used, a false record or statement, to conceal, avoid or decrease an obligation to pay or transmit money or property to the Government." (App. 115).

The statute does not define the term "obligation," but there is direct evidence that it was to be read broadly. In an earlier case, *United States v. Neifert-White Co.*, 390 U.S. 228, 232 (1968), this Court held that the FCA "was

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ch. 497 Title IV, Part V, § 619, 46 Stat. 758 (same); 19 U.S.C. § 1619 (Supp. 1998) (providing informer with 25% of Customs recovery, up to $250,000).

intended to reach all types of fraud, without qualification, that might result in financial loss to the Government." The Senate Report accompanying the 1986 Amendments to the FCA "strongly endorse[d] this interpretation" specifically in connection with the addition of Section 3729(a)(7) to the Act. S. Rep. 99-345, at 19, *reprinted in* 1986 U.S.C.C.A.N. 5266, 5284 ("Senate Report").

D. Proceedings Below

1. The District Court

On November 13, 1997, United States District Judge John D. Holschuh entered an order dismissing this complaint with prejudice for failure to state a claim upon which relief could be granted. (App. 72-73). His opinion acknowledged that the legislative history of the 1986 amendments to the FCA "suggests that the legislators who adopted those amendments favored a more expansive reading of the False Claims Act. . . . " (App. 45). However, he then stated that the "language chosen by Congress . . . was not intended to apply to each and every statement which might conceal from the government the existence of criminal or civil violations to which monetary penalties might attach." (App. 54). He added that Section 3729(a)(7) "is not so broad as to encompass every statutory or regulatory violation which might lead the United States to attempt to assess a fine or other type of monetary penalty against the violator." (App. 62-63).

On November 14, 1997, the day after dismissal, counsel for ATMI learned that, less than two months before

accepting the assignment to this case, Judge Holschuh had been represented in a state criminal proceeding by at least one member of Vorys, Sater, Seymour & Pease ("Vorys, Sater"), the firm that is counsel to the Limited Defendants in this case. Neither Judge Holschuh nor Vorys, Sater disclosed this representation to ATMI. On November 28, 1997, ATMI filed a motion to disqualify Judge Holschuh under 28 U.S.C. § 455(a) and to vacate the judgment of dismissal under Rule 60(b)(6) of the Federal Rules of Civil Procedure in accordance with *Liljeberg v. Health Services Acquisition Corp.*, 486 U.S. 847, 862-864 (1988).

The Limited Defendants opposed this motion, arguing that their counsel's prior representation of Judge Holschuh did not raise any reasonable question about his impartiality because the partner who had represented the judge was not involved in the present case. The Limited's opposition was supported by an affidavit by James A. Arnold, Esq., a partner at Vorys, Sater, which failed to disclose that, in addition to Mr. Arnold, Judge Holschuh was *also* represented by John C. Elam, Esq., a senior partner (formerly the managing partner) at Vorys, Sater. (R. 132, Response to Motion to Disqualify and Vacate Order, Jt. App. below at 1037). On December 15, 1997, ATMI propounded discovery of Vorys, Sater with respect to its appearances before the district court and its representation of Judge Holschuh, in order to develop a full record to support vacatur under the standards established by this Court in *Liljeberg*. The firm refused to submit to discovery, informing Judge Holschuh that the firm was prepared to preserve the "confidences and secrets of its present and former clients."

On December 22, 1997, Judge Holschuh denied ATMI's motion to disqualify, concluding that there was no reasonable basis either to question his impartiality or to require him to vacate his decision. (App. 82). Notwithstanding this determination, Judge Holschuh recused himself "voluntarily," declared that ATMI's request for discovery was therefore moot, but refused to vacate his order of dismissal. (App. 88). Judge Holschuh did not rule on ATMI's Rule 60(b)(6) motion to alter or amend judgment, but suggested that whoever replaced him should conduct a *de novo* review of the merits of the case.

On January 5, 1998, this case was reassigned to Judge Sandra S. Beckwith. On May 21, 1998, Judge Beckwith denied ATMI's motion to vacate. With respect to Judge Holschuh's conflict, she blamed ATMI for not discovering it earlier: "Litigants have a duty to investigate and inform the court of any perceived biases before the court and the parties invest time and expense in a case." (App. 99). With respect to the merits, Judge Beckwith asserted at one point in her opinion that she had undertaken a *de novo* review of the dismissal order, but she then expressly applied a much narrower "clear error" standard of review in denying any relief from Judge Holschuh's order of dismissal: "[Adjustment or vacatur was not] necessary to prevent clear error of law or manifest injustice." (App. 108-109).

2. The Sixth Circuit

The Sixth Circuit affirmed the dismissal. It ruled that the term "obligation" in Section 3729(a)(7) is "ambiguous," (App. 20), and that it was therefore free to

consider "policy implications" in defining the term. *Id.* On that premise, the court expressed concern over "a probable flood of litigation," *id.*, and ignored the "overall intent . . . [of Congress] to encourage more private enforcement suits." Senate Report at 23-24, 1982 U.S.C.C.A.N. at 5288-89. To implement the policy of avoiding a flood of suits, the court ruled that even if an obligation is otherwise fixed and unconditional, it is not an "obligation" within the meaning of Section 3729(a)(7) if it is subject to the enforcement discretion of federal officials. (App. 20-22). The court said that Section 3729(a)(7) covers acknowledged indebtedness, judgment debt, and contract debt (App. 13), but not an obligation that, although fixed and owing in fact, would require an enforcement proceeding: "Contingent obligations – those that will arise only after the exercise of discretion by government actors – are not contemplated by the statute." (App. 19).[3]

The court of appeals refused to review the failure of Judge Holschuh to disclose his relationship with Vorys, Sater, his failure to recuse himself under Section 455(a), and his refusal to vacate his order of dismissal. The court concluded that, in view of its own review of the merits of ATMI's cause of action, "we see no need to decide whether Judge Holschuh faced mandatory recusal, and to

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[3] The court also stated that only obligations sufficiently fixed to be recoverable in a common law debt action are covered by Section 3729(a)(7). (App. 13). In so stating, the court ignored the fact that the customs duties, penalties, and forfeitures described in the complaint were indeed fixed (*see* 3-6, *supra*) and are of kinds that were historically recoverable in actions of debt at common law. *See Bajakajian*, 118 S.Ct. at 2041.

require a third district judge to decide whether ATMI has stated viable claims." (App. 28). The court of appeals did state that Judge Beckwith had erred in asserting that ATMI had a duty to investigate Judge Holschuh's background. (App. 28-29). The court of appeals offered no remedy of any kind for the failure of a district court judge to disclose that a law firm representing a party before him had very recently represented him in a state criminal proceeding, or for his refusal to permit discovery into the circumstances surrounding that representation once it became known.

E. The Position of The Department of Justice

The Department of Justice ("DOJ") elected not to exercise its option under 31 U.S.C. § 3730(b)(2) (App. 117) to intervene in this action. In the district court, DOJ filed two *amicus curiae* briefs generally supporting ATMI and arguing that the FCA should be interpreted expansively. In the court of appeals, DOJ again argued as an *amicus* that Section 3729(a)(7) covers obligations that are due and owing, even if enforcement proceedings may be required. Amicus Brief below at 13-14, 25-26. However, DOJ proposed a quite different limitation (which the court of appeals did not accept) arguing that the term "obligation" in Section 3729(a)(7) applies only to circumstances where "the government had granted the defendants some right, privilege or benefit for which they owed the government money or property." Amicus Brief below at 31. DOJ contended:

> The basic purpose of the False Claims Act is to provide a means of redress to the Treasury for

> loss. . . . If the government has provided no privilege, right or benefit, but is imposing liability on a party solely because that party performed an act that the government has defined as wrongful, the monetary consequences of that wrongful act are *not* actionable under the False Claims Act. . . . It does not apply where the government has granted no right, privilege or benefit and where the false statements at issue conceal only the fact that a defendant engaged in criminal or otherwise unlawful conduct and therefore might properly be subject to fines, penalties, or forfeitures.

Amicus Brief below at 29-30. There was no citation of authority for this position.[4]

REASONS FOR GRANTING THE PETITION

The Court should review the Sixth Circuit's decision because it sharply curtails private and government enforcement actions under the FCA despite broad statutory language and long and clear history to the contrary. The exclusion of unconditional "obligations," whenever a federal official would have discretion not to enforce them, is contrary to the logic of the statute and this Court's instructions for interpreting federal statutes, specifically including this one. Additionally, the Sixth Circuit's refusal to review the district court's conflict of

[4] The importation of merchandise is a privilege, right or benefit conferred by the government on individuals who abide by the Customs laws. *Michelin Tire Corp. v. Wages*, 423 U.S. 276, 294-96 (1976); *New England Butt Co. v. International Trade Comm'n*, 756 F.2d 874, 879 (Fed. Cir. 1985).

interest is out of step with the approach taken in the Fifth and Tenth Circuits and leaves an appearance of serious unfairness that this Court should correct.

I. THE COURT OF APPEALS HAS DECIDED AN IMPORTANT QUESTION OF FEDERAL LAW – THE MEANING OF "OBLIGATION" IN 31 U.S.C. § 3729(a)(7) – IN A DEMONSTRABLY ERRONEOUS WAY

The decision below substantially reduces the reach of Section 3729(a)(7). The court ruled that the section does not apply to "contingent" obligations, which it defined to mean "those that will arise only after the exercise of discretion by government actors," and on this basis it ruled out all "obligations . . . arising from civil and criminal penalties that impose monetary fines after a finding of wrongdoing." (App. 19). In essence, the court limited the section to obligations based on contracts and judgments and carved out all obligations under federal laws that prescribe duties, fines, penalties or other payments for specified actions or inactions by a defendant. In the court of appeals' view, even where the defendant has taken actions that unconditionally trigger an obligation to pay money or property and later makes false statements or reports to conceal that obligation, the FCA does not apply if the pertinent federal officer could elect not to collect that money or property. That miserly interpretation is contrary to the text, history, and purposes of Section 3729(a)(7).[5]

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[5] For clarity, we note two points that may have confused the court of appeals but are not at issue in this case. First, there is no dispute that an obligation must arise first and *then* be

A. The Court of Appeals' Interpretation of Section 3729(a)(7) is Erroneous

Section 3729(a)(7) does not define or in any way limit the meaning of the word "obligation." (App. 114-116). In general, when a word is used in a federal statute without limitation, the courts are expected to read it as written, not to impose policy-based limitations. *Brogan v. United States*, 522 U.S. 398, 408 (1998); *Griffin v. Oceanic Contractors, Inc.*, 458 U.S. 564, 571 (1982). Moreover, in this instance, the legislative history clearly shows that Congress intended a broad and full reading of this key word. In adding Section 3729(a)(7) as part of the 1986 amendments to the FCA, Congress "strongly endorse[d]" this Court's conclusion in *Neifert-White* that the FCA "was intended to reach all types of fraud, *without qualification*, that *might* result in financial loss to the Government." Senate Report at 19, 1986 U.S.C.C.A.N. at 5284 (emphasis added).

The court of appeals confused the breadth of the term "obligation" with ambiguity and improperly assumed

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concealed by a *later* false statement. The FCA does not apply where the false statement itself gave rise to the obligation. (App. 8-9). Here, the Amended Complaint alleged fixed obligations, triggered by unlawful importations, that were *later* concealed by false statements. *See* 3-6, *supra*. Second, this case does not involve obligations that could only be *imposed* as a result of a proceeding not yet conducted. The obligations at issue were triggered by the unlawful importation itself, pursuant to applicable statutory provisions and regulations. Such unconditional obligations that await enforcement are not "contingent" in a legal sense where all of the elements of a cause of action to enforce the obligation are present, but the obligation itself is concealed, or its true size masked, by a false statement or record.

responsibility for narrowing the term. As this Court noted in interpreting the Racketeer Influenced and Corrupt Organizations Act ("RICO"), 18 U.S.C. §§ 1961 *et seq.*:

> "[The] fact that RICO has been applied in situations not expressly anticipated by Congress does not demonstrate ambiguity. It demonstrates breadth." [citations omitted]. . . . [T]his defect – if defect it is – is inherent in the statute as written, and its correction must lie with Congress. It is not for the judiciary to eliminate the private action in situations where Congress has provided it. . . .

Sedima, S.P.R.L. v. Imrex Co., Inc., 473 U.S. 479, 499-500 (1985), *quoting with approval Haroco, Inc. v. Amer. Nat'l Bank & Trust Co. of Chicago*, 747 F.2d 384, 398 (7th Cir. 1984), *aff'd*, 473 U.S. 606 (1985). *Accord: United States v. Monsanto*, 491 U.S. 600, 609 (1989); *Moskal v. United States*, 498 U.S. 103, 111-112 (1990).

With respect to the FCA in particular, this Court has barred use of "policy" considerations to limit the reach of this otherwise broad remedial statute. In *Marcus v. Hess*, the DOJ (as *amicus*) asked the Court to narrow the reach of the FCA by excluding so-called "parasitic" or "copycat suits" – complaints copied by enterprising relators from criminal indictments. The Court refused to do so, holding that the task of narrowing the reach of a broadly framed remedial provision belongs to Congress, no matter how compelling the policy reasons for doing so. 317 U.S. at 544-547. Within a year after this Court's decision in *Marcus v. Hess*, Congress amended the FCA to exclude copycat suits. Act of Dec. 23, 1943, ch. 377 § 1, 57 Stat. 608

(1943) (previously codified at 31 U.S.C. § 3730 (1982) (superseded)).

We do not mean to suggest, of course, that courts are without power to restrict any application of broadly worded remedial statutes. But the plain meaning of the statute controls, except "in rare cases [in which] the literal application of a statute will produce a result demonstrably at odds with the intentions of its drafters. . . ." *Griffin*, 458 U.S. at 571. Neither breadth, nor supposed ambiguity, nor even unexpectedly harsh results, *id.* at 575, provide a justification for a judicial rewrite of a statute based upon policy concerns of the court. The Sixth Circuit should not have created its own limitations on the FCA "no matter how alluring the policy arguments for doing so." *Brogan*, 522 U.S. at 408; *Griffin*, 458 U.S. at 575-76.

The court of appeals' reading is also inconsistent with the central purpose of Section 3729(a)(7), which was to enable the United States to recover obligations *concealed* from it through false records or statements. Concealed obligations necessarily await enforcement because they are unknown to the government. To exclude them from the reach of Section 3729(a)(7) because they are contingent on future enforcement would render the section inapplicable to hidden obligations, the very obligations it was most clearly designed to uncover and remedy.[6] Here, all the elements creating an obligation

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[6] As Justice Story observed in a similar context:

> [I]t can never be permitted that a party who perpetrates a fraud upon the custom-house, and thereby enters his goods upon false invoices and false valuations, and gets a regular delivery thereof upon

were present, and it makes no sense to exclude these obligations precisely because they were successfully concealed. These obligations were not "contingent" in any legal sense; they merely awaited enforcement because they were unknown to the government.[7]

The court of appeals suggests that suits by private citizens should not be allowed to preempt official discretion as to whether or not to enforce an obligation, (App. 19), but that proposition was squarely rejected by this Court in *Marcus v. Hess, supra*. In that case, the United States filed an *amicus curiae* brief arguing that effective law enforcement requires that control be left with the

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> the mere payment of such duties as such false invoices and false valuations require, can avail himself of that very fraud to defeat the purposes of justice. . . . The success of the fraud in evading the vigilance of the public officers, so that it is not discovered until after the goods have passed from their custody does not purge away the forfeiture [or obligation]. . . .

Wood v. United States, 41 U.S. 342, 362 (1842).

[7] The court of appeals appeared uncomfortable with the very idea of using *qui tam* provisions and other informer statutes to recover obligations under the customs laws, but in fact these kinds of provisions have been a principal means of enforcing customs obligations since 1789. *Bajakajian*, 524 U.S. at ___, 18 S.Ct. at 2040 n.18; *Marcus v. Hess*, 317 U.S. at 541 n.4; *Stockwell*, 80 U.S. at 542; *see also* n.1 and n.2, *supra*. Congress is presumed to know the historic context in which it legislates. *Dewsnup v. Timm*, 502 U.S. 410, 419 (1992). The Sixth Circuit's implicit conclusion that Congress could not have intended to include recovery of Customs-based obligations under Section 3729(a)(7) is wholly inconsistent with historic practice with which Congress is presumed to be familiar.

Attorney General, rather than private parties. 317 U.S. at 546-547. This Court observed that the statute placed no pertinent limitations on the right of a person to bring *qui tam* actions, and it refused to impose an exception or limitation by judicial fiat. *Id.* at 547. The Court squarely rejected each of the policy arguments advanced and suggested that they be addressed to Congress. *Id.* at 547-548. The court of appeals cites no authority for the proposition that Congress intended to place obligations, the enforcement of which is subject to official discretion, beyond the scope of Section 3729(a)(7). Indeed, if the Sixth Circuit is correct on this point, courts should also apply the same limitation to false claims under Sections 3729(a)(1)-(4) (App. 114), which also involve the exercise of discretion by government actors. This Court rejected that position in *Marcus v. Hess*, and it should reject the Sixth Circuit's attempt to resurrect it in the context of Section 3729(a)(7). The Sixth Circuit's policy choice has no support in either the language of the statute, its legislative history, or prior rulings by this Court. Indeed, all available authority points in the opposite direction.

Congress empowered private citizens to bring suits to address fraud against the government because it knew that private whistleblowers may learn of fraud of which the government is unaware and hence is not in a position to bring a case on its own. Congress also wanted to add private resources to the arsenal of remedies against fraud, Senate Report at 7, 1986 U.S.C.C.A.N. at 5272, and Congress feared that the government may sometimes be less than fully diligent in its pursuit of fraud. *See Marcus v. Hess*, 317 U.S. at 547. Indeed, Congress authorized private

citizens to prosecute *qui tam* suits even where the government elects not to intervene after the case has been filed, 31 U.S.C. § 3730(b)(2) (App. 117), because it recognized that a private party, motivated by personal gain, is likely to bring additional zeal. *See Hughes Aircraft Co. v. United States ex rel. Schumer*, 520 U.S. 939, 949-50 (1997). The Sixth Circuit's opinion ignores all of these policies underlying Section 3729(a)(7).

B. The Question Is Important

Even as applied in the specific circumstances at issue in this case, the mistake made below is important. The U.S. Customs Service estimates that upwards of 10 billion dollars worth of transshipped textile products from China are unlawfully imported into the United States during a single year. *See* 3, *supra*. Since most of the activity that gives rise to illegal transshipment of goods takes place offshore, Customs is poorly equipped to deal with this problem. By contrast, private parties in the same industry, such as ATMI, are well positioned to recognize unlawful imports and address this activity through suits brought under the *qui tam* provisions of the FCA. The Sixth Circuit's opinion makes it impossible for private parties to assist their government to combat Customs fraud in this way.

The effects of the Sixth Circuit's decision, however, are much broader: the decision has rendered Section 3729(a)(7) inapplicable to all statutory obligations that give rise to monetary obligations to the United States where an official has discretion not to enforce the obligation. It is difficult to conceive of obligations the enforcement of which does not involve official discretion. The

Sixth Circuit has effectively limited the section to judgment debts and contract claims, but it is precisely in the area of concealable statutory violations that private citizen help is needed. By allowing claims only upon judgment and contract obligations, which are by definition already known to the government, and by excluding all obligations the enforcement of which is subject to official discretion, the Sixth Circuit has cut the heart out of the statute. If Congress intended to exclude *all* suits to enforce obligations subject to official discretion, it would have been unnecessary to specifically exclude a subset of such suits arising under the Internal Revenue Code (31 U.S.C. § 3729(e) (App. 116)), which, of course, always involve enforcement discretion. There is no support for the proposition that Congress intended to impose such a limitation on Section 3729(a)(7).

Finally, by drastically narrowing the scope of the term "obligation" in Section 3729(a)(7), the court of appeals has tied the hands of the government as well as potential private relators. Section 3729(a)(7) provides FCA liability for false reports and statements made to conceal an obligation. The liability is the same whether the United States or a private citizen seeks to enforce it. Although this case arises in the *qui tam* context, the Sixth Circuit's decision is not limited to actions filed under the *qui tam* provisions of the FCA. Rather, it applies with equal force to actions initiated by the United States. That is why the United States urged the court of appeals not to adopt the interpretation it selected. Amicus Brief below at 13-14, 25-26.

II. THE COURT SHOULD GRANT THE PETITION TO REVIEW THE COURT OF APPEALS' HANDLING OF THE DISTRICT JUDGE'S CONFLICT OF INTEREST

Judge Holschuh had a serious conflict of interest in this case: an important, very recent, personal relationship, as client, with the law firm representing a principal set of defendants. He did not reveal that conflict, and when it came to light shortly after he had rendered a decision, he avoided discovery of the details and declined to accept mandatory recusal, instead recommending *de novo* review by a second judge. Judge Beckwith, the second district judge, stated that she had given the matter *de novo* review, and the court of appeals echoed that statement, but her opinion makes clear that she wrongly faulted ATMI for failure to learn of the problem earlier (App. 97-98), and that she only reviewed the outcome for "clear error" or "manifest injustice." (App. 108-109). The court of appeals, agreeing with Judge Holschuh on the merits, essentially ignored the conflict problem, except to correct Judge Beckwith's statement faulting ATMI. (App. 27-29). To say the least, Judge Holschuh's "impartiality might reasonably be questioned," 28 U.S.C. § 455(a), and the entire episode lacks the appearance of fairness.

Under these circumstances, appellate review should not have been limited to the merits. The court of appeals refused to consider whether vacatur was required because of the conflict of interest, reasoning that because it agreed with Judge Holschuh on the merits any conflict of interest was harmless. (App. 27-29). However, that ruling conflicts with this Court's instructions in *Liljeberg*, *supra*, that the reviewing court should consider "the risk

of injustice to the parties in the particular case, the risk that the denial of relief will produce injustice in other cases, and the risk of undermining the public's confidence in the judicial process." 486 U.S. at 863. An important interpretation of federal law was rendered in this case without full consideration by an unbiased district judge. The court of appeals should at the very least have considered ATMI's arguments that allowing that decision to stand is unfair to ATMI in this case, sets a bad precedent for future cases, and is likely to undermine public confidence in the integrity of the judicial process. 486 U.S. at 860, 863.

"Harmless error" is not the appropriate standard for dealing with a palpable judicial conflict of interest. As the Fifth Circuit explained at an earlier stage in *Liljeberg*, "the appearance of impropriety is not lessened by the fact that the litigation would have come out the same anyway." *Health Services Acquisition Corp. v. Liljeberg*, 796 F.2d 796, 801 (5th Cir. 1986), *aff'd*, 486 U.S. 847 (1988). The Tenth Circuit similarly rejected the notion that a *de novo* review of the merits allows a circuit court to abrogate its duty to exercise supervisory authority over district court judges in *Harris v. Champion*, 15 F.3d 1538, 1570-72 (10th Cir. 1994).[8] The Sixth Circuit's opinion in this case is out of

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[8] *Harris* involved a situation where one judge of a three-judge district court panel hearing *habeas corpus* motions should have, but failed to, recuse himself in a number of cases, consolidated on appeal. Although the circuit court did not vacate the panel's unanimous rulings, the court did review the failure to recuse, made clear that its "application of harmless error is unique to the procedural posture" involved, and instructed the errant judge to recuse himself in similar

step with the approach being followed in the Fifth and Tenth Circuits and should be reviewed by this Court under its supervisory responsibility over the conduct of the lower courts.

CONCLUSION

The petition for a writ of certiorari should be granted.

Respectfully submitted,

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situations henceforth. 15 F.3d at 1570-72. Additionally, citing *Harris* and *Liljeberg*, the court made plain in its unpublished decision in *Clark v. City of Draper*, No. 96-4006, 1997 U.S. App. LEXIS 6421, *7 (10th Cir. 1997), that the approach of the Tenth Circuit is that *"de novo* review in no way removes the appearance of impropriety."

AMERICAN TEXTILE MANUFACTURERS INSTITUTE, INC., Plaintiff-Appellant,

v.

THE LIMITED, INC., et al.; Tarrant Apparel Group, et al., Defendants-Appellees.

No. 98-3889.

United States Court of Appeals, Sixth Circuit.

Argued: Aug. 12, 1999.

Decided and Filed: Sept. 14, 1999.

Douglas N. Letter (argued and briefed), Sandra Wien Simon, Richard A. Olderman (briefed), U.S. Department of Justice, Civil Division, Appellate Staff, Washington, D.C., for Amicus Curiae.

Paul D. Cullen (argued and briefed), Diana E. Stein and Joseph Black (briefed), Cullen Law Firm, Washington, D.C., Ann Lugbill and James B. Helmer, Jr. (briefed), Helmer, Lugbill, Martins & Morgan, L.P.A., Cincinnati, Ohio, for Plaintiff-Appellant.

Michael J. Canter (briefed), James E. Phillips, Vorys, Sater, Seymour & Pease, Columbus, Ohio, John T. Boese (argued and briefed), Fried, Frank, Harris, Shriver & Jacobson, Washington, D.C., for Defendant-Appellee The Limited, Inc.

David J. Young (briefed), Squire, Sanders & Dempsey, L.L.P., Columbus, Ohio, for Defendant-Appellee Tarrant Apparel Group.

Before: KEITH, BOGGS, and CLAY, Circuit Judges.

OPINION

BOGGS, Circuit Judge.

The American Textile Manufacturers Institute filed a qui tam action against several defendants, alleging that the defendants submitted false claims to the government to avoid payment of fines, duties, and liquidated damages for the illegal transshipment of imported textiles. A United States District Judge dismissed the complaint for failure to state a claim, but later recused himself because of his prior representation by a member of the firm representing one of the defendants. A second judge took over the case and declined to vacate, alter, or amend the prior judgment. ATMI appealed, and we affirm.

I

In September 1996, the American Textile Manufacturers Institute ("ATMI") filed a complaint in the United States District Court for the Central District of California, naming as defendants The Limited, Inc. and several subsidiary corporations (referred to as the "Limited defendants"), Tarrant Apparel Group and a subsidiary corporation (the "Tarrant defendants"), and two California citizens, principal shareholders of the Tarrant Apparel Group. ATMI sued on behalf of the United States, claiming that the defendants violated 31 U.S.C. § 3729(a)(7), a provision of the False Claims Act. The government declined to intervene.

ATMI, the national trade association of the domestic textile industry, complained that the defendants engaged in transshipping and mislabeling of the country of origin

of textile and apparel products. ATMI alleged that its investigations revealed that the defendants

> engaged in a pattern or practice of trade pursuant to which articles of apparel produced in the People's Republic of China have been transhipped to Hong Kong or Macau; have been falsely labeled as the products of Hong Kong or Macau; and have been knowingly represented to be the products of Hong Kong or Macau in official entry documents submitted to Customs by or on behalf of said Defendants.

ATMI contended that the defendants filed false entry documents "used to enter or introduce textile and apparel products into the commerce of the United States that were not entitled to admission [because of textile quotas] and were not marked with the true country of origin."

ATMI alleged that the defendants' practices exposed them to liability under the following statutes, and that the filing of false documents concealed from the government the defendants' liability:

> (1) 18 U.S.C. § 545, prohibiting the smuggling of goods into the United States, the importation of illegal goods, and the use of false customs documents.
>
> (2) 19 U.S.C. § 1595a(b), penalizing those persons who assist in the importation of goods "contrary to law."
>
> (3) 19 U.S.C. § 1592, penalizing the making of negligent, grossly negligent, or fraudulent material omissions or false material statements in connection with the importation of any merchandise into United States commerce.

(4) 19 U.S.C. § 1623 (and the implementing regulations in 19 C.F.R. Part 113), governing customs bonds, and requiring the return of improperly-marked merchandise, and permitting the United States to obtain liquidated damages for violations of the bonds. *See* 19 C.F.R. § 113.62(l).

(5) 19 U.S.C. § 1304(h), imposing a ten percent ad valorem marking duty on goods bearing false country-of-origin markings.

(6) 15 U.S.C. §§ 45(m), 70a(a) & 70b(b)(4), branding as unfair competition the importation of misbranded textile fiber, and subjecting violators to civil penalties of up to $10,000 per violation.

ATMI contended that each count adequately alleged a violation of 31 U.S.C. § 3729(a)(7), which imposes liability on a person who "knowingly makes, uses, or causes to be made or used, a false record or statement to conceal, avoid, or decrease an obligation to pay or transmit money or property to the Government." If the defendants had truthfully disclosed the country of origin, ATMI reasoned, they would not face liability for violating the six statutes listed in the complaint. Thus, according to ATMI, the False Claims Act applied, because the defendants made false statements to avoid the "obligations" to pay money (fines, liquidated damages, and duties) arising from their violations of the customs laws.

The defendants sought to change venue to Columbus, Ohio, the principal place of business for most of the defendants. The defendants also moved to dismiss the complaint for failure to state a claim, arguing, inter alia, that the False Claims Act referred to existing obligations

to the United States, and not to as-yet-unproved violations of statutes. In June 1997, District Judge Harry Hupp granted the motion to transfer venue to the United States District Court for the Southern District of Ohio, where the court permitted the parties to supplement their briefing to concentrate on Sixth Circuit – rather than Ninth Circuit – law. The United States filed an amicus curiae brief to argue that the comprehensive administrative scheme of the customs laws did not preempt private causes of action under the False Claims Act.

On November 13, 1997, District Judge Holschuh granted the defendants' motion to dismiss the complaint. After discussing ATMI's claims and the meaning of "obligation" as used by the False Claims Act, Judge Holschuh concluded that 31 U.S.C. § 3729(a)(7) did not "encompass a claim based on the submission of false records to avoid payment to the United States of forfeitures or fine." "So drastic an expansion in the scope of the False Claims Act, through the use of language which strongly implies that there be some type of financial relationship between the defendant and the United States which is subject to being affected by an act of concealment or avoidance, could not reasonably have been intended [by Congress]."

On November 28, 1997, ATMI moved to disqualify Judge Holschuh and to vacate the order of dismissal, and, in the alternative, to alter or amend the judgment. In the motion to disqualify, ATMI explained that it learned on November 14 that James E. Arnold, a partner with Vorys, Sater, Seymour and Pease, had represented Judge

Holschuh in a state proceeding in May 1997. Other attorneys from Vorys, Sater represented The Limited in ATMI's action under the False Claims Act.

On December 22, 1997, Judge Holschuh issued an order concluding that a reasonable person with knowledge of the surrounding circumstances would believe that the judge had acted impartially in the proceedings. Nevertheless, Judge Holschuh decided voluntarily to recuse himself. He refused to vacate, alter, or amend the judgment, however, although he urged the new judge to review de novo the defendants' motion to dismiss. Judge Beckwith assumed responsibility for the case, ruled that Judge Holschuh's recusal did not mandate that she vacate his judgment, and held that ATMI did not show that Judge Holschuh's November 1997 order worked a manifest injustice or contained a clear error of law. *See United States ex rel. American Textile Mfrs. Institute, Inc. v. The Limited, Inc.*, 179 F.R.D. 541 (S.D.Ohio 1997). Thus, she denied the motion to alter or amend the judgment. ATMI appealed, and the United States participated at oral argument as amicus curiae. We turn to the merits of the appeal.

II

A

Congress passed the original False Claims Act in 1863 to respond to Civil War fraud. The statute prohibits the knowing submission of false "claims" to the government, and the Supreme Court has given the statute an expansive reading. *See, e.g., United States v. Neifert-White Co.*, 390 U.S. 228, 232-33, 88 S.Ct. 959, 19 L.Ed.2d 1061

(1968). The Act covers "all fraudulent attempts to cause the Government to pay out sums of money." *Id.* at 233, 88 S.Ct. 959. In 1986, Congress amended the Act; the amendments included a provision to extend the Act to cover "reverse false claims." *See* 31 U.S.C. § 3729(a)(7). The new language prohibits the use of false statements or records to "conceal, avoid, or decrease an obligation to pay or transmit money or property to the Government." *Ibid.* Now, the Act declares that any person who:

> (1) knowingly presents, or causes to be presented, to an officer or employee of the United States Government or a member of the Armed Forces of the United States a false or fraudulent claim for payment or approval;
>
> (2) knowingly makes, uses, or causes to be made or used, a false record or statement to get a false or fraudulent claim paid or approved by the Government;
>
> (3) conspires to defraud the Government by getting a false or fraudulent claim allowed or paid;
>
> (4) has possession, custody, or control of property or money used, or to be used, by the Government and, intending to defraud the Government or willfully to conceal the property, delivers, or causes to be delivered, less property than the amount for which the person receives a certificate or receipt;
>
> (5) authorized to make or deliver a document certifying receipt of property used, or to be used, by the Government and, intending to defraud the Government, makes or delivers the receipt without completely knowing that the information on the receipt is true;

> (6) knowingly buys, or receives as a pledge of an obligation or debt, public property from an officer or employee of the Government, or a member of the Armed Forces, who lawfully may not sell or pledge the property; or
>
> (7) knowingly makes, uses, or causes to be made or used, a false record or statement to conceal, avoid, or decrease an obligation to pay or transmit money or property to the Government,
>
> is liable to the United States Government for a civil penalty of not less than $5,000 and not more than $10,000, plus 3 times the amount of damages which the Government sustains because of the act of that person. . . .

This appeal involves the meaning of "obligation" in 31 U.S.C. § 3729(a)(7).

ATMI's complaint alleges that the defendants violated customs laws and implementing regulations. The joint appendix does not suggest that the government has alleged wrongdoing, let alone that the government has found that the defendants broke any law. Rather, ATMI contends that the defendants violated laws and made false statements to avoid discovery and the consequences. ATMI contends that each customs violation created an obligation to pay money to the government, and that the allegedly-false entry documents served to "conceal, avoid, or decrease" the obligations.

Judge Holschuh characterized the question as

> whether a person who violates some statute or regulation that subjects that person to a possible monetary fine or forfeiture of property and who

> then makes a false statement to conceal that offense is liable under the False Claims Act for having concealed the existence of an "obligation" to the government by means of a false statement.

(J.A. 111). Judge Holschuh discussed the text, history, and purpose of the reverse false claim amendment. Although he did not resolve the scope of the meaning of "obligation," he appears to have decided that a reverse false claim exists only when there is an attempt to avoid a pre-existing financial liability between a defendant and the government. "It is sufficient in the present case for the Court to find . . . that the language of § 3729(a)(7) is not so broad as to encompass every statutory or regulatory violation which might lead the United States to attempt to assess a fine or other type of monetary penalty against the violator." After engaging in de novo review, Judge Beckwith refused to alter or amend the opinion. *See The Limited*, 179 F.R.D. at 550 n. 11.

B

As a preliminary matter, we note that, whatever the scope of the phrase "obligation to pay or transmit money or property to the Government," 31 U.S.C. § 3729(a)(7), a plaintiff may not state a reverse false claim unless the pertinent obligation attached before the defendant made or used the false record or statement. Section 3729(a)(7) prohibits the use of a false statement to "conceal, avoid, or decrease an obligation," and does not use the phrasing "that create an obligation."[1] Where an obligation arises if

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[1] Presumably, it uses "avoid" in the sense of "shirk."

and only if a defendant makes a false statement or files a false claim (e.g., a law prohibiting the filing of false customs documents), an action under the False Claims Act will not lie (although the government can obtain redress by bringing an action under the customs statute, or perhaps by prosecuting misstatements under 18 U.S.C. § 1001). *Cf. United States ex rel. Hopper v. Anton*, 91 F.3d 1261, 1266 (9th Cir.1996) (discussing false certification claims, not reverse false claims) ("Violations of laws, rules, or regulations alone do not create a cause of action under the FCA. It is the false certification of compliance which creates liability when certification is a prerequisite to obtaining a government benefit."), *cert. denied*, 519 U.S. 1115, 117 S.Ct. 958, 136 L.Ed.2d 844 (1997). Keeping the preceding limitation in mind, we turn to the meaning of "obligation" in the statute.

Although few courts have interpreted 31 U.S.C. § 3729(a)(7), the Eighth Circuit has rejected an expansive reading of the provision. In *United States v. Q International Courier, Inc.*, 131 F.3d 770 (8th Cir.1997), the court interpreted "obligation" after the government prosecuted a reverse false claim action against a courier service alleged to have illegally avoided paying full domestic postage for mail sent from Barbados to United States destinations. *See id.* at 772-74. The court concluded that the regulation at issue does not

> oblige the violator to pay the postage that might have been collected by the Postal Service; it merely sets the limit of a potential penalty against the violator at the amount of postage that might have been collected. A potential penalty, on its own, does not create a common-law

> debt. A debt, and thus an obligation under the meaning of the False Claims Act, must be for a fixed sum that is immediately due. This regulation merely provides a range of penalties that might be assessed; it does not create an immediate duty to pay a specific sum.

Id. at 774. The court set forth its interpretation of § 3729(a)(7):

> To recover under the False Claims Act, we believe that the United States must demonstrate that it was owed a specific, legal obligation at the time that the alleged false record or statement was made, used, or caused to be made or used. The obligation cannot be merely a potential liability: instead, in order to be subject to the penalties of the False Claims Act, a defendant must have had a present duty to pay money or property that was created by a statute, regulation, contract, judgment, or acknowledgment of indebtedness. The duty, in other words, must have been an obligation in the nature of those that gave rise to actions of debt at common law for money or things owed.

Id. at 773.[2] *See also United States ex rel. Lamers v. City of Green Bay*, 998 F.Supp. 971, 997-98 (E.D.Wis.1998)

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[2] Also, in the panel opinion in *United States v. Pemco Aeroplex, Inc.*, 166 F.3d 1311 (11th Cir.1999), reh'g en banc granted, opinion vacated, 179 F.3d 1327 (11th Cir.1999), the court faced a reverse false claim action alleging that the defendant falsely recorded stock numbers and thereby purchased aircraft wings from the government at outrageously low prices. *See id.* at 1312. The panel agreed with the Eighth Circuit that "Section 3729(a)(7) of the False Claims Act requires a specific, legal obligation to pay or to transmit money or property, at the time a false statement is made." *Id.* at 1315 (Hull,

(approvingly citing, without adopting, Q International, and permitting reverse false claims only where the defendant has "an immediate, recognizable obligation" to pay the government), aff'd, 168 F.3d 1013 (7th Cir.1999); *United States ex rel. S. Prawer & Co. v. Verrill & Dana*, 962 F.Supp. 206, 209 (D.Me.1997) (holding that § 3729(a)(7) does not cover "possible indeterminate future . . . liabilit [y]") ("Whether an obligation would exist depends on the outcome of litigation pursuing the alleged statutory violation."); *United States ex rel. S. Prawer & Co. v. Verrill & Dana*, 946 F.Supp. 87, 95, 94 n. 12 (D.Me.1996) (defining "obligation" as arising only from "a specific contract remedy, a judgment, or an acknowledgment of indebtedness") ("Otherwise, however, there appears to be no way to define the scope of such cases, which would seem to be as broad as any lawyer's creative impulses in defining a possible claim in the first place."). *But see Pickens v. Kanawha River Towing*, 916 F.Supp. 702, 705 (S.D.Ohio 1996) (finding a valid reverse false claim in the allegation that, by failing to note in its vessel's logs the discharge of pollution, the defendant avoided paying fines to the government); *United States ex rel. Stevens v. McGinnis, Inc.*, No. C-1-93-442, 1994 WL 799421, at *6 (S.D.Ohio Oct. 26, 1994) (unpublished) (permitting, on facts related to those

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J., dissenting). Judge Hull dissented on other grounds, however, contending that the majority erred in finding that "Pemco's filing of the inventory schedule did not create a specific, legal obligation or a present duty to pay money, and the government's complaint does not detail any other type of reverse false claim." *Id.* at 1314-15 (Hatchett, C.J.). Rather, Hull claimed that Pemco had a contractual obligation to return the property. *See id.* at 1316 (Hull, J., dissenting). The 11th Circuit vacated the decision and will rehear the case en banc.

in *Pickens*, a reverse false claim action "where a defendant has omitted to disclose information to the Government that concealed or avoided its obligation to pay the cleanup costs for its discharges and the associated fines for intentional dumping").

We agree with the reasoning of the Eighth Circuit. Thus, we hold that a reverse false claim action cannot proceed without proof that the defendant made a false record or statement at a time that the defendant owed to the government an obligation sufficiently certain to give rise to an action of debt at common law. Whatever its scope, the False Claims Act clearly encompasses specific and legal duties to pay or transmit money or property to the government. A defendant risks liability when making a false statement to conceal, avoid or decrease obligations such as his prior acknowledgment of indebtedness, a final court or administrative judgment that the defendant owes money or property to the government, or a contractual duty to pay or transmit money or property to the government.

Our review of the statute's text, legislative history, and most reasonable interpretation leads us to this conclusion. Recourse to plain meaning does not quickly resolve the matter. "Obligation" has several meanings:

> A generic word, derived from the Latin substantive "obligatio," having many, wide, and varied meanings, according to the context in which it is used. That which a person is bound to do or forbear; any duty imposed by law, promise, contract, relations of society, courtesy, kindness, etc. Law or duty binding parties to perform their agreement. An undertaking to perform. That

> which constitutes a legal or moral duty and which renders a person liable to coercion and punishment for neglecting it; a word of broad meaning, and the particular meaning intended is to be gained by consideration of its context. An obligation or debt may exist by reason of a judgment as well as an express contract, in either case there being a legal duty on the part of the one bound to comply with the promise. Liabilities created by contract or law (i.e. judgments). As legal term word originally meant a sealed bond, but it now extends to any certain written promise to pay money or do a specific thing. A formal and binding agreement or acknowledgment of a liability to pay a certain sum or do a certain thing. The binding power of a vow, promise, oath, or contract, or of law, civil, political, or moral, independent of a promise; that which constitutes legal or moral duty.

BLACK'S LAW DICTIONARY 968-69 (5th ed.1979) (citations omitted). "Obligation" must have some limit, however. *See, e.g., United States ex rel. S. Prawer & Co. v. Verrill & Dana,* 962 F.Supp. 206, 208 (D.Me.1997) ("The unbounded scope of the relators' argument is demonstrated in their assertion that even a moral obligation is sufficient for a reverse false claim."); cf. BLACK'S LAW DICTIONARY 363 (5th ed.1979) (defining "debt") ("[Debt] may even mean a moral or honorary obligation, unenforceable by legal action.").

The Act defines "claim," *see* 31 U.S.C. § 3729(c), but it does not define "obligation." Given the Act's use of "claim" in most provisions of § 3729(a), the Act's employment of "obligation" in § 3729(a)(6) & (7) suggests that Congress intended a different, and more limited, meaning

for "obligation." "Claims" encompass requests for payment not only based on contracts, but also because of the many privileges and benefits doled out by the government. When seen in context, the Act's use of "obligation" suggests a more limited meaning:

> (6) knowingly buys, or receives as a pledge of an obligation or debt, public property from an officer or employee of the Government, or a member of the Armed Forces, who lawfully may not sell or pledge the property; or
>
> (7) knowingly makes, uses, or causes to be made or used, a false record or statement to conceal, avoid, or decrease an obligation to pay or transmit money or property to the Government. . . .

31 U.S.C. § 3729(a) (emphases added). *Cf. United States v. Rivera*, 55 F.3d 703, 712 (1st Cir.1995) (discussing the meaning of "claim," not "obligation," and implicitly distinguishing the terms) ("The key inquiry is thus whether the demand for payment, whether or not it gives rise to an unconditional legal obligation to pay right away, has the practical effect of inducing the government to suffer immediate financial harm.") (emphasis added).

The legislative history of the 1986 amendment accords with the preceding interpretation and the distinction between "claim" and "obligation." In its Neifert-White opinion, which antedates the 1986 amendments, the Court interpreted "claims" and concluded that the statute "reaches beyond 'claims' which might be legally enforced, to all fraudulent attempts to cause the Government to pay out sums of money." 390 U.S. at 233, 88 S.Ct. 959. The 1986 Senate Report uses similar language to describe the reach of the pre-1986 False Claims Act. *See*

S.REP. NO. 99-345, at 9, reprinted in 1986 U.S.C.C.A.N. 5266, 5274. Many courts had refused to apply the Act to efforts to avoid paying the government, however, so Congress amended the Act to include reverse false claims. The amendment's history reflects a concern with efforts to avoid paying "money owed" – a phrase that evokes Black's Law Dictionary's definition of "liabilities created by contracts or laws (i.e. judgments)" – and the history cites as examples cases involving disputes over taxes, contracts, and leases. *See* S.REP. NO. 99-345, at 15, 18, reprinted in 1986 U.S.C.C.A.N. 5266, 5280, 5283.

We have already mentioned those obligations clearly encompassed by the statute: acknowledgements of indebtedness, judgments, and breaches of contract. The claims made by ATMI rely on more attenuated obligations, however, so we must continue to explore the scope of "obligation" as used in the False Claims Act. A statute or regulation might also impose a duty to pay or transmit property, and breaches of such a duty might expose a defendant to liability under the reverse false claims provision. For example, in its decision in Q International, the Eighth Circuit confronted the case of a mail courier allegedly engaged in an illegal international remailing scheme. The court refused to find liability under 31 U.S.C. § 3729(a)(7), holding that, although the plaintiff might have shown that the defendant engaged in fraud, the plaintiff failed to show that the defendant violated Postal regulations imposing an obligation to pay postage. *See Q Int'l*, 131 F.3d at 773-74.

The case of *United States v. Raymond & Whitcomb Co.*, 53 F.Supp.2d 436 (S.D.N.Y.1999), complements that of Q International. In *Raymond & Whitcomb*, the court found

that the defendant, a commercial travel agent, impermissibly used a favorable non-profit mailing rate and thereby violated an obligation sufficient to incur reverse false claims liability. Where the regulations at issue in *Q International* merely released the Postal Service from an obligation not to obtain payment from those impermissibly using international rates, the regulations at issue in *Raymond & Whitcomb* imposed an affirmative obligation on mailers to pay the proper domestic postage. *See id.* at 445-47. One treatise (admittedly authored by an attorney who represented The Limited in the instant matter) anticipated the distinction, explaining that:

> Such obligations [those actionable under the reverse false claims provision] exist, for example, in logging and concession contracts on public lands (where the contractor owes the United States a percentage of gross or net income) or in an established amount for the price of stamps or other postal services, which are essentially contractual in nature. . . . While the precise amount may be uncertain, these are obligations or liabilities, arising under a contract or quasi contract that existed at the time the false statement is made.

JOHN T. BOESE, CIVIL FALSE CLAIMS AND QUI TAM ACTIONS 2-41-42 (1999 Supp.).

Although we do not decide the matter, we think that the history of the 1986 amendments suggest that Congress may well have intended reverse false claims liability to extend to obligations created by statute or regulation, at least where the statute or regulation imposes an obligation "essentially contractual in nature," such as the imposition of the requirement that those

using the Postal Service pay the appropriate rate. The implications of such liability give us pause, however, as such an interpretation has broad potential reach.[3] The Federal Government charges for many services apart from mail delivery, and establishes universally-applicable rates for each service. For example, the National Air and Space Museum in Washington, D.C. contains the Samuel P. Langley IMAX Theatre, which shows films on an impressively-large screen. Museum-goers must pay for the privilege, and the theater provides discounts for "Youth" (categorized as those aged 2-17) and "Seniors" (categorized as those aged 55 and higher). *See Smithsonian, National Air & Space Museum, Langley Show Times* (visited August 26, 1999) <http://www.nasm.edu/nasm/IMAX/IMAXtimes.html.> If a fifty-four-year-old malfeasor lied to the cashier to obtain a discount, a suspicious fellow patron could bring a reverse false claim action against the wrongdoer, who would find the fraudulently-obtained admission discount outweighed by the imposition of a civil penalty of not less than $5,000.

We leave for another day the question of the IMAX Theatre, however, because the plaintiffs in the instant

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[3] 31 U.S.C. § 3730 provides incentives for private parties to police actionable frauds, as it allows them to bring actions under the False Claims Act, and to receive up to 30 percent of the proceeds of the action. 31 U.S.C. § 3730(d)(2) also provides for reimbursement of reasonable attorneys' fees and costs. The preceding statutory sections, combined with the mandate of 31 U.S.C. § 3729(a), which imposes a civil penalty of $5,000 to $10,000 for each violation and awards treble damages to the government, give plaintiffs powerful incentives to lodge such actions.

case found their claims on purported obligations that fall outside the scope of "obligation" as used in the False Claims Act, even if we interpret the Act to permit those claims contemplated in the preceding two paragraphs. A defendant does not execute a reverse false claim by engaging in behavior that might or might not result in the creation of an obligation to pay or transmit money or property to the government. Contingent obligations – those that will arise only after the exercise of discretion by government actors – are not contemplated by the statute. Examples of contingent obligations include those arising from civil and criminal penalties that impose monetary fines after a finding of wrongdoing: as opposed to quasi-contractual obligations created by statute or regulation (such as the imposition of a standard mailing rate), contingent obligations (such as the imposition of a civil penalty for an antitrust violation) attach only after the exercise of administrative or prosecutorial discretion, and often after a selection from a range of penalties.

When the 1986 amendment's legislative history discusses disputes over whether the pre-amendment Act covered reverse false claims, it mentions "attempts to defeat or reduce the amount of a claim or potential claim by the United States against [a person]." S.REP. NO. 99-345, at 18, reprinted in 1986 U.S.C.C.A.N. 5266, 5283. Although one could use "potential claim" to argue that Congress intended the amendment to reach possible, or contingent, liabilities (as opposed to those confirmed by judgments), the context suggests the Senate Report offhandedly used "claim" to reflect legal claims based on contracts or leases: the Report follows the mention of

"potential claim" by discussing cases involving fraudulent tax returns, government contracts, and leases with the government. *See ibid.* The Report does not mention, and probably did not consider, false statements made to avoid possible civil or criminal liability.

Our holding that a defendant's behavior regarding a contingent obligation cannot engender a reverse false claim action draws support from a consideration of the consequences of the competing interpretation. Of course, a court may not allow policy considerations to trump the plain language of a statute. *See, e.g., Brogan v. United States*, 522 U.S. 398, ___, 118 S.Ct. 805, 810, 139 L.Ed.2d 830 (1998). Here, however, Congress has used an ambiguous term, and considering policy implications helps to inform us what Congress intended "obligation" to mean, in light of the probable flood of litigation that would follow from an overly expansive interpretation of the reverse false claims provision. *Cf. United States v. American Heart Research Found.*, 996 F.2d 7, 10 (1st Cir.1993) (construing a different provision of the False Claims Act, interpreting the scope of "claim") ("But it is one thing to construe ambiguous language broadly in accord with a remedial purpose; it is quite another matter to stretch language beyond normal usage or understanding, when the natural reading matches the very problem that concerned Congress at the time the statute was enacted.") (citation and internal quotation marks omitted).

In ATMI's case, the defendants did not have a contract or lease with the government, and did not ask for money or benefits from the government. The government has not brought a criminal or civil action against the defendants, and thus has no judgment against them.

Rather, the defendants stand accused of making false statements to avoid paying customs duties, fines, and taxes. If the reverse false claims provision encompasses the defendants' actions, it has incredible scope, permitting suits against any person who makes a false statement to the federal government that he did not commit a statutory or regulatory violation that might have led to the imposition of a fine, payment of liquidated damages, imposition of a tax, or forfeiture of property.

> [T]his expansive interpretation of Section (a)(7), if adopted broadly, would have had the potential to significantly expand False Claims Act jurisdiction into areas not involving the expenditure of Federal funds. The significance of this expansion can be conceptualized by imagining a motorist who, stopped for speeding in a Federal park, blurts out, "But, officer, I was only doing the speed limit!" Assuming the motorist's statement to be false, this attempt to avoid a $75 speeding ticket, payment to which the United States is entitled, could generate liability for a $10,000 penalty under the False Claims Act.

JOHN T. BOESE, CIVIL FALSE CLAIMS AND QUI TAM ACTIONS 2-39 (1999 Supp.). Vivid as it is, Boese's example understates the breadth of reverse false claims liability under ATMI's interpretation. Boese discusses a federal crime (i.e., speeding in a Federal park) that is prosecuted almost automatically and with a near-guarantee of attendant financial obligation (i.e., the fine). ATMI asks us to permit reverse false claims based on allegedly false statements made to conceal liability under criminal statutes that prosecutors enforce only after exercising discretion, and that, if violated, will not necessarily give

rise to "an obligation to pay or transmit money or property to the government." For example, ATMI charges that the defendants made false statements to conceal their liability under 18 U.S.C. § 545, a statute prohibiting the smuggling of goods into the United States and permitting the imposition of a fine, a term of imprisonment, or both. Under that interpretation, reverse false claims liability would attach to any person making any false statement to conceal, avoid, or decrease his potential criminal liability under a law that lists among a range of penalties the imposition of a fine.[4]

The expansive interpretation is flawed because not only does it require a judicial determination of whether the government would have exercised its discretion not to pursue relief, but it also would require consideration of whether the government would have sought relief satisfying the False Claims Act's linguistic trigger of "money or property" (fines, taxes, and so forth). Under this interpretation, a court would also have to calculate the amount of the financial penalty (taking into account concerns of retribution and deterrence, in addition to restitution) – a far cry from the often-rote calculations

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[4] 18 U.S.C. § 2113 permits the imposition of a fine or term of imprisonment for those convicted of federal bank robbery charges. Imagine a bank robber captured by police and interrogated as a suspect. If an officer asks, "Do you know who robbed the bank?" and the robber denies knowledge, or blames another, or makes up an alibi, the robber would incur reverse false claim liability under ATMI's interpretation. If prosecuted, if convicted, and if fined, he would have an obligation to pay money to the government. His response to the police serves to conceal the obligation.

accompanying government contract disputes (the heartland of claims under the Act). Rejecting the expansive interpretation does not reward wrongdoers, of course, as they still face penalties for violating the underlying statute (the speeding motorist will have to pay the ticket, if he does not contest it and win).

Additionally, the rejection of the expansive interpretation accords with the position of the United States as advanced in its 1991 filings in a case in the Eastern District of California, *United States ex rel. Sequoia Orange Co. v. Oxnard Lemon Co.*, CV. No. F-91-194 OWW. Sequoia alleged that Oxnard submitted false reports to the Lemon Administrative Committee to avoid paying statutory forfeitures and assessments, and to ship more lemons than allowed by the Committee's regulations. The government contended that Sequoia did not state a claim under 31 U.S.C. § 3729(a)(7): "an attempt to circumvent an obligation to pay created solely as the result of a violation of an administrative enforcement statute does not constitute a cognizable claim under the Act." "False claims submitted by individuals or entities seeking to avoid payment to the Government of administrative fines, penalties or forfeitures (OSHA, FAA, SEC, etc.), or criminal fines imposed pursuant to Title 18 of the United States Code, are not the stuff of False Claims Act lawsuits. . . . " The government made similar arguments in its reply brief, and contended that an expansive interpretation would interfere with federal regulatory enforcement schemes, and permit companies to use qui tam litigation to harass competitors.[5]

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[5] The district court rejected the government's interpretation, however. *See United States ex rel. Sequoia Orange Co. v.*

The government submitted an amicus brief in ATMI's case and departed from its 1991 position. The amicus brief urges this court to affirm the district court's judgment, but asks that this court hold that the district court adopted an overly-restrictive interpretation of the statute. The government contends that:

> [T]he "reverse false claims" provision encompasses within its scope those obligations owed to the government (under statute, regulation, contract, or quasi-contract) arising from the provision of some privilege, right or benefit in return for which the recipient owes money or property. If the government has provided no privilege, right or benefit, but is imposing liability on a party solely because that party performed an act that the government has defined as wrongful, the monetary consequences of that wrongful act are not actionable under the FCA. Accordingly, the Act applies to false statements made to avoid payment of contractual obligations [even in the absence of a judgment], or monetary obligations, such as customs duties or user fees, imposed by statute or regulation. It does not apply, however, where the government has granted no right, privilege, or benefit and where the false statements at issue conceal only the fact that the defendant engaged in criminal or otherwise unlawful conduct and therefore might properly be subject to fines, penalties, or forfeitures.

Oxnard Lemon Co., 1992 WL 795477, at *6 (E.D.Cal. May 4, 1992).

The government observes that the Act also applies to "obligations" reduced to judgments and to "obligations" incorporated in government contracts.

Although the government's position has some force, we fear the hazards of attempting to determine the meaning of "right, privilege, or benefit," especially in light of Congress's extensive regulation of international and interstate commerce. We reiterate our holding, and summarize, by concluding that 31 U.S.C. § 3729(a)'s definition of "obligation" certainly includes those arising from acknowledgements of indebtedness, final judgments, and breaches of government contracts, and that the definition certainly does not include those contingent obligations that arise only because the government has prohibited an act, or arising after the exercise of government discretion. We leave for a more appropriate case the status of those obligations arising from the provision of "rights, privileges, or benefits," and those obligations created by statute or regulation that are "essentially contractual in nature."

C

With the preceding guidelines in mind, we turn to ATMI's specific claims, and hold that the district court properly dismissed the complaint. ATMI brought six counts against the defendants, contending that the defendants' filing of false documents concealed from the government the defendants' liability under several statutes. Counts one (18 U.S.C. § 545), two (19 U.S.C. § 1595a(b)), three (19 U.S.C. § 1592), and six (15 U.S.C. §§ 45(m),

70a(a) & 70b(b)(4)) rely on the theory of contigent obligations, rejected *supra* in Part II.B. Count four (19 U.S.C. § 1623 and 19 C.F.R. Part 113), involving the posting of a customs bond, also involves an obligation that arises only after a defendant breaks the law (by mismarking the country of origin), and implicates a monetary obligation that arises only after administrative investigation and a decision to notify the defendant that the government seeks payment of the liquidated damages it believes are due under the bond.

Count five, alleging that the defendants filed false documents to conceal liability under 19 U.S.C. § 1304(h), presents the most difficulty, as it involves a provision applying a ten percent ad valorem marking duty to goods having false country-of-origin markings. We affirm, however, because the marking duty applies only when a defendant engages in conduct that the statute defines as wrongful. The government contrasts the marking duty with "standard customs duties that are payable in exchange for a right to import goods into the United States." The distinction appears rather fine. One court has found that wrongful use of a (domestic) postage nonprofit rate yields a "clear actual obligation to pay the deficiency," *United States v. Raymond & Whitcomb Co.*, 53 F.Supp.2d 436, 1999 WL 430552, at *9 (S.D.N.Y. June 19, 1999), and the marking duty does not seem too far removed. In light of a recent decision by the Federal Circuit, however, the government's distinction appears tenable: unlike the domestic postal duty and most customs duties, the ad valorem duty applies if and only if the importer makes a false statement:

> [19 U.S.C.] Section 1592(a) prohibits misrepresentations resulting from misconduct – fraud, gross negligence, or negligence. Thus, the actions that violate § 1592(a) are the acts of fraudulently or negligently mismarking imported goods. If the act of culpably mismarking the goods deprived the government of duties, for example, if the goods were marked with a country of origin having a lower duty than the country from which the goods actually originated, then those duties of which the government was deprived are of the type whose tender is required for prior disclosure treatment. We hold that the 10 percent ad valorem mismarking duties do not fall into this category.
>
> The act of culpably mismarking goods cannot be said to have deprived the government of the 10 percent ad valorem duty assessed under 1304(f). To the contrary, but for the mismarkings (followed by the failure to export, destroy, or remark the articles in accordance with section 1304), the duty could not have arisen.

Pentax Corp. v. Robison, 125 F.3d 1457, 1463 (Fed.Cir.1997), amended on reh'g by 135 F.3d 760 (Fed.Cir.1998). Thus, the district court's judgment on count five comports with our observation above at pages 8-9 that "a plaintiff may not state a reverse false claim unless the pertinent obligation attached before the defendant made or used the false record or statement."

III

Because this appeal required us to discern the meaning of "obligation," we engaged in plenary review of the district court's final order. *Cf., e.g., In re Griggs*, 965 F.2d

54, 56 (6th Cir.1992) ("Because this case presents an issue of statutory interpretation, which is a question of law, our review of the district court's decision is *de novo.*"). In light of our disposition of the case as a matter of law, and given District Judge Beckwith's *de novo* review of District Judge Holschuh's decision, we see no need to decide whether Judge Holschuh faced mandatory recusal, and to require a third district judge to decide whether ATMI has stated viable claims.

Nevertheless, we write to clarify that a litigant's duty to investigate the facts of his case does not include a mandate for investigations into a judge's impartiality. Judge Beckwith erred by suggesting otherwise. After proclaiming that "[t]he strategy employed by Relator [filing the recusal motion two weeks after receiving an unfavorable dispositive ruling] is questionable at best, and the Court refuses to reward Relator or encourage this trend," she concluded that subsection of her opinion by stating that "[l]itigants have a duty to investigate and inform the court of any perceived biases before the court and the parties invest time and expense in a case. Relator has posited no reason for the failure to make a timely inquiry into Judge Holschuh's background." *United States ex rel. American Textile Mfrs. Institute Inc. v. The Limited, Inc.*, 179 F.R.D. 541, 546 (S.D.Ohio 1997).

We believe instead that litigants (and, of course, their attorneys) should assume the impartiality of the presiding judge, rather than pore through the judge's private affairs and financial matters. Further, judges have an ethical duty to "disclose on the record information which the judge believes the parties or their lawyers might

consider relevant to the question of disqualification." *Porter v. Singletary*, 49 F.3d 1483, 1489 (11th Cir.1995). "[B]oth litigants and counsel should be able to rely upon judges to comply with their own Canons of Ethics." *Ibid.* In ATMI's case, Judge Holschuh possibly did not consider the matter sufficiently relevant to merit disclosure, but his nondisclosure did not vest in ATMI a duty to investigate him.

IV

The judgment of the district court is AFFIRMED.

IN THE UNITED STATES DISTRICT COURT
FOR THE SOUTHERN DISTRICT OF OHIO
EASTERN DIVISION

United States of America ex rel. American Textile Manufacturers Institute, Inc.,	:	
Plaintiff/Relator,	:	Case No. C2-97-776
v.	:	JUDGE HOLSCHUH
The Limited, Inc., et al.,	:	
Defendants.	:	

OPINION AND ORDER

(Filed Nov. 13, 1997)

This case was filed by the American Textile Manufacturers Institute, which, according to the complaint, is the national trade association of the domestic textile industry. The defendants are a number of corporations and individuals whose business includes importing manufactured textile goods, *i.e.* clothing. Relator complains that the defendants either arranged for or knew about the fact that certain lots of imported clothing were incorrectly marked – that is, that the labels and import documents said they were manufactured in Hong Kong or Macau instead of the People's Republic of China, where they were really made. Relator asserts that when defendants submitted inaccurate "entry documents" to United States Customs officials during the importation process, defendants incurred liability to the United States under the False Claims Act ("FCA"), 31 U.S.C. §§3729 *et seq.* Relator is pursuing its claim under the *qui tam* provisions of that

statute, 31 U.S.C. §3730(b), which allow a private individual to pursue the government's claims under the FCA and to share in any recovery.[1]

Relator filed its complaint in the United States District Court for the Central District of California, and the case was transferred to this Court at defendants' request. While that request was under advisement in California, defendants moved to dismiss the complaint. After the case arrived here, the parties were given an opportunity to supplement their briefing on the motions to dismiss in order to focus more precisely on Sixth Circuit, rather than Ninth Circuit, precedent. The issues raised by defendants' motions to dismiss the complaint have been exhaustively briefed. Additionally, although defendants had originally requested oral argument, they withdrew that request in a letter to the Court dated September 4, 1997. For the following reasons, the Court concludes that the complaint fails to state a claim under the False Claims Act and must therefore be dismissed under Fed. R. Civ. P. 12(b)(6).

I.

When considering a motion to dismiss pursuant to Fed. R. Civ. P. 12(b)(6), a court must construe the complaint in the light most favorable to the plaintiff and accept all well-pleaded material allegations in the complaint as true. *Scheuer v. Rhodes*, 416 U.S. 232, 236 (1974);

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[1] The government elected not to intervene and proceed with the action and so notified the Court pursuant to 31 U.S.C. §3730(b)(4)(B).

Roth Steel Products v. Sharon Steel Corp., 705 F.2d 134, 155 (6th Cir. 1983). When determining the sufficiency of a complaint in the face of a motion to dismiss, the court must apply the principle that "a complaint should not be dismissed for failure to state a claim unless it appears beyond a doubt that the plaintiff can prove no set of facts in support of his claim which would entitle him to relief." *Conley v. Gibson*, 355 U.S. 41, 45-46 (1957). *See also, McLain v. Real Estate Bd. of New Orleans, Inc.*, 444 U.S. 232 (1980); *Windsor v. The Tennessean*, 719 F.2d 155, 158 (6th Cir. 1983), *cert. denied*, 469 U.S. 826 (1984).

A motion to dismiss under Rule 12(b)(6) is directed solely to the complaint itself. *Roth Steel Products*, 705 F.2d at 155. Consequently, the Court must focus on whether the claimant is entitled to offer evidence to support the claims, rather than whether the plaintiff will ultimately prevail. *Scheuer*, 416 U.S. at 236. A federal court cannot consider extrinsic evidence in determining whether a complaint states a claim upon which relief can be granted. *Roth Steel Products*, 705 F.2d at 155. The Court will grant a defendant's motion to dismiss under Fed. R. Civ. P. 12(b)(6) if the complaint is without merit because of an absence of law to support a claim of the type made, or of facts sufficient to make a valid claim, or if on the face of the complaint there is an insurmountable bar to relief indicating that the plaintiff does not have a claim. *See generally Rauch v. Day & Night Mfg. Corp.*, 576 F.2d 697, 702 (6th Cir. 1978)

II.

The First Amended Complaint filed on March 21, 1997 is lengthy and detailed. Rather than repeat all of relator's factual assertions, the Court will simply summarize the crucial allegations of the complaint in order to provide a framework for the legal discussion which follows.

This case apparently arose out of an investigation conducted by relator into the garment manufacturing practices of the defendants or their overseas affiliates, particularly those located in the People's Republic of China, Hong Kong, and Macau. Although somewhat more detail is necessary to understand the legal issues posed by the motions to dismiss, it is fair to state that the general matter about which relator complains is the manufacture of garments in the People's Republic of China and the "trans-shipment" of those garments to Hong Kong or Macau where labels were attached to the garments indicating that they were manufactured in one of those two locations. Once, as relator alleges, the garments were improperly marked concerning their country of origin, they were imported into the United States through the use of documents stating that they had been manufactured in either Hong Kong or Macau. The primary purpose of this scheme, according to relator, was to avoid quotas placed on the importation of garments from the People's Republic of China. If the goods had been properly marked, they would have been refused by Customs officials because the quota for importing goods manufactured in the People's Republic of China would have been exceeded.

Describing one of several instances set forth in the complaint will illustrate this point. According to relator, one of the major suppliers of garments to the Limited and its subsidiaries, many of which are defendants in this action, is Gaddy Garment Factory, located in Hong Kong. During most of 1995, Gaddy had agreed to produce in excess of 30,000 garments per month for the Limited defendants. Relator initiated surveillance at Gaddy's Hong Kong facility, and was unable to observe any substantial manufacturing occurring there. Given the volume of garments which Gaddy was obligated to produce, relator contends that at least 80 people had to be involved in the manufacturing process, but Gaddy's Hong Kong operation was simply not that large. Rather, relator contends that Gaddy had subsidiaries located in the Guangdong Province in China which manufactured the garments and shipped them to Hong Kong in cartons with the words "Made in Hong Kong" printed on them. Then, when the garments were imported into the United States, importation documents were prepared stating that the garments had been manufactured in Hong Kong rather than in China. Gaddy is only one of a number of foreign garment makers which allegedly engaged in the same type of activity either at the direct request of, or with the knowledge of, one or more of the defendants.

According to the complaint, when garments are imported into this country, a group of documents known as "entry documents" must be executed. They include, according to paragraph 142 of the complaint, a "Customs Form 7501," commercial invoices, declarations required

by 19 C.F.R. §12.130(f), and other documents.[2] These documents are required to identify the "country of origin" of the imported goods because, among other reasons, there are quotas on the amount of goods that can be imported from certain foreign countries, including the People's Republic of China. According to relator, in 1995 and 1996 the defendants filed literally thousands of entry documents falsely representing that manufactured textile goods originated in either Hong Kong or Macau when, in fact, the actual country of origin was the People's Republic of China.

The complaint asserts that this type of improper importation and labeling violates six different statutory or regulatory schemes. In order to understand relator's theory of FCA liability, it is important to understand the way these six sets of statutes and regulations operate. Therefore, the Court will describe each one in some detail.

Count One invokes 18 U.S.C. §545. That statute, which is part of the criminal code, is entitled "Smuggling Goods into the United States," and provides that anyone who "makes out or passes, or attempts to pass, through the customhouse any false . . . or fraudulent invoice, or other document or paper," or who "brings into the United States, any merchandise contrary to law" or who

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[2] 19 C.F.R. §12.130(f), a regulation of the United States Customs Service, Department of the Treasury, requires that all importations of certain textiles and textile products be accompanied by appropriate declarations set forth in the regulation regarding the country of origin of the articles.

"receives . . . or in any manner facilitates the transportation . . . or sale of such merchandise after importation" is subject to a fine and a jail term of up to five years. Section 545 also provides that any merchandise unlawfully smuggled into the United States, or the value of that merchandise, is to be forfeited to the United States by the person responsible for the smuggling.

There is no private civil remedy available under 18 U.S.C. §545. Central to Count One and all other counts of the complaint is relator's assertion that, by importing the improperly marked goods and using the false documents to do so, defendants were able to conceal from the United States the existence of a monetary liability – in this case, the fines and forfeitures that the United States could have assessed under §545. In other words, had defendants not falsified the entry documents for the improperly-labeled garments, the United States would have learned of the unlawful importation of the garments, because it is a violation of the customs laws to import a garment which bears an incorrect designation of the country of origin. At that point, the government would have been entitled, under §545, to assess a monetary penalty against the defendants equal to the value of the imported merchandise. It is relator's position that such an assessment is an "obligation" to the United States which defendants "concealed" by way of false statements, and, according to relator, defendants thereby violated 31 U.S.C. §3729(a)(7), a subsection of the False Claims Act which allegedly forbids such concealment.

Count Two is conceptually no different from Count One, other than its reliance on a different statutory section as the "predicate offense" of the False Claims Act

claim. 19 U.S.C. §1595a provides for forfeitures and other penalties for violating specified sections of the Tariff Act of 1930. Among other things, it allows the seizure and forfeiture of any means by which an article is imported into the United States contrary to law, and it also provides for monetary penalties equal to the value of the article or articles introduced against anyone who "directs, assists financially or otherwise, or is in any way concerned in any unlawful activity" described in §1595a(a), *i.e.* the unlawful importation of articles into the United States. 19 U.S.C. §1595a(c) also permits the merchandise to be seized and forfeited, although if the importing violation deals only with the classification or value of merchandise and not its admissibility into the country, no seizure can occur except as permitted by 19 U.S.C. §1592. Again, relator claims that defendants violated the FCA by using false import documents to conceal an alleged monetary liability under this statute.

19 U.S.C. §1592 is the basis for Count Three of the complaint. That provision of the Tariff Act of 1930, which is entitled "Penalties for Fraud, Gross Negligence and Negligence," prohibits the introduction of merchandise into the United States by means of "any document . . . or information, written or oral statement, or act which is material and false. . . . " When the Customs Service reasonably believes that such a false statement has been made in connection with the importation of merchandise, it is authorized to issue a notice of intention to issue a claim for a monetary penalty and, after certain procedures are followed, if it finds a violation, it can assess a range of penalties depending upon whether the violation

found was fraudulent, grossly negligent, or simply negligent. Seizures of merchandise are also authorized under specific circumstances by 19 U.S.C. §1592(c)(6). These are all monetary penalties that defendants allegedly concealed from the United States through the use of false entry documents.

19 U.S.C. §1623 and 19 C.F.R. Part 113 are the statutory and regulatory bases for Count Four. 19 U.S.C. §1623, also part of the Tariff Act of 1930, allows the Secretary of the Treasury or the Customs Service to require that bond be posted in connection with the importation of merchandise. Relator alleges that bonds were filed by the defendants for all of their garment importations, and that under these bonds defendants are required, *inter alia*, to "make or complete an entry to enable Customs to determine whether the applicable requirements of law and regulation are met." (Complaint, ¶176). Regulations found in 19 C.F.R. Part 113 require individuals or organizations who have posted such a bond to return improperly marked merchandise to the Customs Service once it is learned that the marking is improper. Relator alleges that the defendants violated the terms of their bonds, and that if it had not been for the false entry documents, the United States could have assessed monetary penalties, including liquidated damages equal to the value of the merchandise. *See* 19 C.F.R. §113.62, which states, *inter alia*, that the obligors on a bond agree to pay liquidated damages equal to the value of the merchandise for committing specified bond violations.

In Count Five, relator identifies 19 U.S.C. §1304 as yet another source of duties allegedly violated by the defendants. 19 U.S.C. §1304, also part of the Tariff Act of 1930, provides that every article of foreign origin imported in the United States must be marked in a way that will permit the ultimate purchaser of the article in the United States to identify the article's country of origin. If the article is not so marked, the government is entitled to collect an additional ten percent *ad valorem* duty. As in the other counts, relator alleges that by concealing the improper marking of the imported garments, defendants were also able to conceal the existence of facts that would cause the United States to impose this duty.

Finally, Count Six asserts that the defendants' unlawful importation of misbranded articles into the United States violates both the Federal Trade Commission Act, 15 U.S.C. §45(l), and the Textile Fiber Products Identification Act, 15 U.S.C. §70A(a).These acts provide for civil penalties of up to $10,000 per violation. In a manner similar to that alleged in Counts One through Five, relator contends that by concealing these statutory violations through the use of false entry documents, defendants concealed and avoided their obligation to pay these civil penalties to the United States.

Under the legal standard applicable to motions to dismiss, the Court is required to accept as true relator's allegations concerning the manufacture of garments in the People's Republic of China, followed by the mismarking of these garments as having been manufactured in either Hong Kong or Macau and the importation of the garments through the use of entry documents which state falsely that Hong Kong or Macau were the countries of

origin of these garments. Although legal conclusions contained in a complaint need not be accepted at face value, the Court's independent review of the statutes and regulations in question confirms that it is at least possible that the actions described in the complaint violate one or more provisions of federal law which permit the United States to assess a monetary penalty of some type, including a civil or criminal fine.

The primary question raised by the motions to dismiss (although there are others) is whether a person who violates some statute or regulation that subjects that person to a possible monetary fine or forfeiture of property and who then makes a false statement to conceal that offense is liable under the False Claims Act for having concealed the existence of an "obligation" to the government by means of a false statement.[3] Relator contends that this type of conduct is actionable under one subsection of the False Claims Act, 31 U.S.C. §3729(a)(7).

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[3] Defendants argue, as noted *infra*, that the alleged false statements in the entry documents in the present case would be the basis for *creating* the potential penalties which relator regards as "obligations" to the government and not statements to *conceal* any such obligations. Relator contends that liability attached when the improperly labeled merchandise arrived in this country and that the allegedly false entry documents were submitted to conceal liability. The issue framed by the Court views relator's claim in the light most favorable to relator; that is, the Court assumes only for purposes of this decision that the complaint sufficiently alleges both an unlawful act to which monetary penalties may attach, and a separate act of making a false statement in order to conceal the commission of the initial unlawful act.

III.

A.

The motions to dismiss filed by the two separate sets of defendants (the "Limited defendants" and the "Tarrant defendants") assert the following. First, all defendants argue that a False Claims Act violation has to involve something more than the failure to comply with some other statute or regulation; that is, "[m]ere regulatory violations do not give rise to a viable FCA action." *United States ex rel. Hopper v. Anton*, 91 F.3d 1261, 1267 (9th Cir. 1996), *cert. denied* 117 S.Ct. 958 (1997). Essentially, defendants contend that the same conduct that allegedly violated some other statute or regulation, such as the use of false entry documents or the mismarking of garments, cannot also be the FCA violation; in order to violate the FCA, at a minimum, some independent false statement concealing the underlying statutory or regulatory violation is required.

Even if the Court were to conclude, as relator contends, that making and presenting false entry documents is sufficiently independent of the underlying conduct (the illegal importation of mismarked goods) to constitute a separate false statement that could be actionable under the FCA, defendants also assert that relator's theory of liability is deficient because in order for §3729(a)(7) to be violated, there must be an "obligation" that is owed to the United States and which is concealed by means of a false statement. Defendants argue that an "obligation" exists only under limited circumstances, such as when there is a clear contractual liability owed to the United

States, or when a judgment has been entered on a statutory or common law claim. Because, according to defendants, the "obligations" that arise from the mere violation of a federal statute or regulation are essentially inchoate and largely indeterminate until the United States undertakes some action to enforce the law, such as the actual assessment of a penalty or the imposition of a fine or duty, they do not fall within the purview of §3729(a)(7).

Defendants make two other arguments as well. First, they assert that the complaint does not plead the allegedly fraudulent conduct with the particularity required by Fed.R.Civ.P. 9(b). Second, the two individual defendants, both of whom are part of the Tarrant group of defendants, argue that the complaint does not set forth any facts that would make them individually liable for the alleged misdeeds of their corporate employers. Because the Court concludes, for the reasons that follow, that the complaint fails to state a claim for relief under the FCA, it is not necessary to address these two issues.

B.

Because this case involves an issue of statutory interpretation, the Court begins its discussion with the words of the statute. 31 U.S.C. §3729(a)(7) reads as follows:

> "(a) **Liability for certain acts.** – Any person who –
>
> (7) knowingly makes, uses, or causes to be made or used, a false record or statement to conceal, avoid, or decrease an obligation to pay or transmit money or property to the Government,

> is liable to the United States Government for a civil penalty of not less than $5,000 and not more than $10,000, plus three times the amount of damages which the Government sustains because of the act of that person. . . . "

Although §3729(a)(7), like the other subsections of Section 3729(a), provides for recovery only by the United States government, 31 U.S.C. §3730(b) permits private persons to file civil actions for violations of §3729, and §3730(d) permits a private person to receive a reasonable amount of compensation for collecting the civil penalty[4] and damages owing to the United States, which is to be not less than 25% and not more than 30% of the proceeds of the action plus an award for expenses necessarily incurred, including attorneys' fees. Relator has proceeded under these statutory provisions, and, at least for the moment, there is no dispute about its standing to prosecute the claim. Rather, the focus of the pending motions to dismiss is whether there is a claim to be prosecuted. In order to answer that question, the Court must explore in some depth the text, history, and purpose of §3729(a)(7).

As originally enacted, the False Claims Act did not contain any provision making persons liable for attempting to avoid or conceal an obligation to pay or transmit money to the government. Rather,

> "The False Claims Act was adopted in 1863 and signed into law by President Abraham Lincoln in order to combat rampant fraud in civil war

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[4] The "civil penalty" referred to in §3730(d) clearly refers to the civil penalty described in §3729(a), and not a civil penalty that might potentially be assessed under other statutes such as the ones involved in this case.

> defense contracts. Originally the act provided for both civil and criminal penalties assessed against one who is found to knowingly have submitted a false claim to the Government."

Senate Report No. 99-345, False Claims Amendment Act of 1986, *reprinted* at 1986 *U.S. Code Congressional and Administrative News*, 5266, 5273; *see also United States ex rel. Hopper v. Anton*, 91 F.3d at 1265-66 ("The FCA was enacted during the Civil War with the purpose of forfending widespread fraud by government contractors who were submitting inflated invoices and shipping faulty goods to the government.").

Under that formulation, which persisted until certain amendments were adopted in 1986, a prerequisite for the filing of a civil action to recover penalties and damages under the False Claims Act was that the defendant had submitted some type of affirmative claim for payment to the government. Although prior to 1986 a few court decisions had allowed so-called "reverse false claim" actions[5] to be brought, *see e.g., Smith v. United States*, 287 F.2d 299 (5th Cir. 1961) and *United States v. Douglas*, 626 F.Supp. 621 (E.D. Va. 1985), other courts had concluded that the type of fraud which did not produce an overpayment of funds from the government, but rather resulted in an underpayment of funds to the government, was not covered by the False Claims Act because no "claim for payment" was being presented. *See, e.g., United States v.*

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[5] A "reverse false claim" refers generally to a false statement made to conceal, avoid or decrease an obligation to pay money to the government, as contrasted with a false statement made to obtain money from the government.

American Heart Research Foundation, 996 F.2d 7, 10 (1st Cir. 1993) (refusing to apply the pre-1986 version of the False Claims Act to an alleged fraudulent request for reduced postal rates, noting that "the Supreme Court has thrice affirmed [the] natural reading [of the word 'claim'] and emphasized that a 'claim' in this context refers to one for money or property. . . . "). Although the legislative history of the 1986 amendments suggests that the legislators who adopted those amendments favored a more expansive reading of the False Claims Act as it existed prior to 1986, it is also clear that the primary reason for the enactment of §3729(a)(7) was precisely to codify the principle that a "reverse false claim" was actionable.

The key word used by Congress when it adopted §3729(a)(7) to address the "reverse false claim" issue is the word "obligation." Under §3729(a)(7), it is only fraudulent acts taken to conceal or avoid an "obligation" owed to the government which are actionable. The parties have devoted a significant portion of their briefs to a discussion of what the word "obligation" means. In the Court's view, "obligation" is one of those words whose meaning can vary depending upon the context within which it is used. It is not clear, either from the remaining language used in §3729(a)(7) or the language of the False Claims Act as a whole, exactly what sense of the word Congress intended. Strictly construed, an "obligation" can refer only to a pre-existing right to payment based upon clear contractual language or arising from a judgment rendered by a court of law. More loosely construed, it can refer to any set of circumstances under which the government could conceivably make a demand for payment by the alleged obligor, regardless of the legal basis for that

demand. Because the language of the statute does not really address the breadth of the meaning to be given to this key term, the Court believes that a resort to both legislative history and the decisional landscape is necessary in order to ascertain the most likely sense in which Congress intended the word "obligation," as it is used in §3729(a)(7), to be interpreted.

The Court has already discussed some of the relevant legislative history. It seems clear that Congress had identified a specific problem in the decisional law relating to "reverse false claims" and wanted to address that problem through section (a)(7). The two cases which the Senate Report cites with approval, *United States v. Douglas* and *Smith v. United States,* involved situations where a party had a contractual obligation to the United States and, through false reporting, sought to reduce the amount of money which it was otherwise obligated to pay. The cases criticized in the Senate Report, in which the courts refused to recognize a "reverse false claim" as actionable, involved similar factual scenarios, such as where contract or lease arrangements had been entered into with the United States. The Report also refers to cases holding that the filing of a fraudulent federal tax return in order to reduce or avoid the payment of income tax, would, but for the statutory exemption for tax claims, be the type of "reverse false claim" which would be addressed by the amendment. Tax cases were the only illustration given of cases where the obligation to pay money to the United States arose by virtue of the operation of a statute or regulation as opposed to some voluntary arrangement under which the defendant agreed to pay money to the United States. The legislative history is

completely silent on the question of whether new subsection (a)(7) was intended to reach situations involving a possible obligation to pay the government fines or other penalties that could be imposed for a violation of some specific statute or regulation, as contrasted with the Internal Revenue Code which itself imposes a present, ongoing obligation on all citizens to pay the government tax money due the government, without regard to any possible obligation to pay fines or other penalties as a result of a failure to pay required taxes.

There are few judicial decisions which directly or indirectly address this issue. Defendants rely heavily on *United States ex rel. S. Prawer & Co. v. Verrill & Dana*, 946 F.Supp. 87 (D. Me. 1996), a case which supports defendants' view that the word "obligation" was intended to have a very narrow meaning. *Prawer* held that the word "obligation" refers only to a "legal obligation," which, in turn, requires that there be a specific contract in place creating the obligation, an acknowledgment of indebtedness by the defendant, or a money judgment rendered in the government's favor. Relator, on the other hand, points to decisions such as *Pickens v. Kanawha River Towing*, 916 F.Supp. 702 (S.D. Ohio 1996) (Spiegel, J.), which hold that the creation of a document such as a ship's log which contains a false statement that the vessel's owner has not discharged pollutants – an act which could bring about the imposition of monetary penalties – is actionable under the False Claims Act if the document is reviewed by the government. A similar result was reached by Judge Weber in *United States ex rel. Stevens v. McGinnis*, No. C-1-93-442 (S.D. Ohio Oct. 26, 1994), 1994 WL 799421 (unreported).

Interestingly, although the *Prawer* case, on the one hand, and the *Pickens* and *McGinnis* cases, on the other hand, reach diametrically opposite conclusions, they do so based upon the same legislative history. In *Prawer,* the court traced the use of similar language throughout the history of the False Claims Act, reviewed the language of the legislative history which included the use of the phrase "money owed" to the government, and found a restrictive interpretation of the term "obligation" logical, because otherwise the scope of the remedy created by the 1986 amendments would seem to be as broad as any lawyer's creative impulses in defining a possible claim. . . . *Prawer,* 946 F. Supp. at 94-95 n.13. Both *Pickens* and *McGinnis* appear to assume, without extensive discussion, that the commission of some act such as the discharge of pollutants into a river which might, at some future date, if uncovered by the United States and processed through proper channels, give rise to the imposition of a monetary penalty, immediately created an "obligation" which a false record could then serve to conceal. This was based upon Congress' purported intent in extending the False Claims Act to reach essentially any species of fraud against the government, an intent consistent with the Supreme Court's pronouncement in *United States v. Neifert-White Co.,* 390 U.S. 228, 232 (1968) that the False Claims Act "was intended to reach all types of fraud, without qualification, that might result in financial loss to the government." Of the three decisions, only *Prawer* seems to be concerned with the impact of an interpretation of the False Claims Act which is expansive enough to reach the types of situations dealt with in the *McGinnis* and *Pickens* cases, and which is present here.

Although these three decisions appear to be the ones most closely on point, it is helpful to discuss other court decisions as well which have some bearing on the extent to which relator's construction of §3729(a)(7) is a reasonable one. In particular, the Court finds helpful decisions which deal with the question of whether a party who has undoubtedly submitted a claim for payment, and undoubtedly included some type of false statement within that claim, committed a violation of the False Claims Act even though there did not appear to be a direct relationship between the false statement and either the amount of money to be paid pursuant to the claim or the existence of the obligation to pay money on account of the claim. Several examples will serve to illustrate this point.

Courts have struggled with the concept of imposing liability under the FCA for certain types of false or misleading statements made by a person who has submitted a claim for payment to the United States. If the false statement directly causes a payment to be made, or directly causes a payment to be larger than it otherwise would have been, §§3729(a)(1) and (2) – which proscribe the presentation of a "false or fraudulent payment or claim" and the use of a "false record or statement to get a false or fraudulent claim paid" – are clearly and properly invoked as the basis for FCA liability. In fact, this is the archetypal FCA lawsuit. *See, e.g., United States ex rel. Hopper v. Anton*, 91 F.3d at 1266 ("The archetypal *qui tam* FCA action is filed by an insider at a private company who discovers his employer has overcharged under a government contract."). However, it is frequently the case

that a false statement or record appears in the documentation for a claim for payment, but plays no part in the government's decision to pay the claim or the decision as to how much to pay. At that point, courts differ as to whether Congress intended to extend the "false claim" provisions of the FCA beyond the archetypal case.

In *United States ex rel. Pogue v. American Healthcorp., Inc.*, 914 F.Supp. 1507 (M.D. Tenn. 1996), the defendants, health care providers, had allegedly referred Medicare and Medicaid patients to another provider in violation of federal anti-kickback and self-referral statutes. They then presented claims to the government for Medicare and Medicaid payments. It appeared that the amount of the claims, and the entitlement to be paid for the services rendered, were not affected by the illegal referral of the patients. However, because the payees were deemed to have implicitly represented, in their claims, that no violations of Medicare or Medicaid statutes or regulations had occurred, the *qui tam* relator alleged that the claims for payment were "fraudulent claims" within the meaning of the False Claims Act.

The *Pogue* court discussed extensively competing lines of cases addressing this same scenario, some of which held that the False Claims Act was implicated by the submission of a claim for payment containing a false statement unrelated either to the obligation to pay money or the amount to be paid, and others holding that it was not. The Court also noted that, in contrast to the language quoted in the Senate Report from *United States v. Neifert-White Co.* concerning the broad reach of the False Claims Act, the Supreme Court had also stated, in *United States v. McNinch*, 356 U.S. 595, 599 (1958), that the False Claims

Act "was not designed to reach every kind of fraud practiced on the government." The Court concluded that although the False Claims Act "was not intended to operate as a stalking horse for enforcement of every statute, rule or regulation" giving rise to some type of monetary claim by the government, it was nonetheless implicated by a defendant who "engaged in . . . fraudulent conduct with the purpose of inducing payment from the government." *Id.* at 1513. It permitted the claim to go forward only because relator "alleged that the government would not have paid the claim submitted by Defendants if it had been aware of the alleged kickback and self-referral violations" – in other words, that had the government known the truth, it would have withheld payment even though there did not appear to be a direct causal connection between the type of fraud engaged in and the amount being claimed for services. The Court left open the possibility that if the alleged fraudulent conduct "was not committed with the purpose of inducing payment from the government, that conduct does not operate to taint [defendants'] . . . claims and render the claims false or fraudulent under the False Claims Act." *Id.*

The same issue was discussed by the District Court in *United States ex rel. Thompson v. Columbia/HCA Health Care*, 938 F.Supp. 399 (S.D. Tex. 1996), *rev'd* ___ F.3d ___ (5th Cir. October 23, 1997), 1997 WL 619314. The District Court had adopted a more restrictive reading of the False Claims Act, (1) finding that the claim itself had to be false or fraudulent before the FCA was implicated; (2) defining a false or fraudulent claim to be a "claim[ ] or a claim amount[ ] that the government would not have had to pay but for the fraud"; and (3) concluding that the FCA

was not "intended to be used as a private enforcement device for the Medicare anti-kickback statute and Stark laws [relating to self-referral]." *Thompson*, 938 F. Supp. at 405. The Court of Appeals reversed, but only because it construed the complaint to have alleged that compliance with the anti-kickback and Stark laws was, in fact, a prerequisite to payment. Although the case was remanded for further factual development on that issue, the Court of Appeals reaffirmed its earlier holding in *United States ex rel. Weinberger v. Equifax, Inc.*, 557 F.2d 456, 461 (5th Cir. 1977), *cert. denied* 434 U.S. 1035 (1978) that "[t]he False Claims Act is not an enforcement device for [other federal laws such as] the Anti-Pinkerton Act."

Pogue and *Thompson* both discussed the Court of Claims' decision in *Ab-Tech Constr. v. United States*, 31 Fed. Cl. 429 (1994), *aff'd* 57 F.3d 1084 (Fed. Cir. 1995), a case also cited by the parties here. *Ab-Tech* involved the submission of payment vouchers which, in the Court's words, "represented an implied certification by *Ab-Tech* of its continuing adherence to the requirements for participation in" the government program at issue. Had the alleged violations of those requirements been disclosed in the payment certifications, it appeared that the United States would not have paid additional money to *Ab-Tech* because it would not have been an eligible participant in the program. Because these misrepresentations "caused the government to pay out funds in the mistaken belief that it was furthering the aims of the . . . program," the court concluded that a false claim had been submitted within the meaning of the FCA. *Id.* at 434. Both *Pogue* and *Ab-Tech* appear to be premised on the underlying assumption that, even when the government receives fair value

for its money, if the money is paid to a person who, because of some other misfeasance, is not actually entitled to receive it – for example, by being an ineligible participant in the government program – the government has paid out money under circumstances where, absent the fraud, it would not have done so, and the FCA has thereby been violated.

Although the issue in these cases was whether the defendant had submitted a fraudulent claim and thereby incurred liability under sections (a)(1) and (a)(2) of the FCA, under the interpretation of §3729(a)(7) urged by relator here, these would have been easy cases. Regardless of whether the false statements submitted as a part of the claim for payment had any impact on the timing or amount of the payment, they would have qualified as "false record[s] or statement[s] to conceal, avoid, or decrease an obligation to pay . . . the Government" – namely the obligation to pay the civil or criminal penalty which attached to the underlying misconduct. Had truthful statements been made – that is, had the defendants in *Pogue* and *Thompson* disclosed their violations of the federal anti-kickback and self-referral statutes – the government would have been able to pursue civil and criminal monetary penalties called for by those statutes. These penalties would, according to relator here, be "obligations" that were "concealed" by the claims submitted, and liability under §3729(a)(7) would be the obvious result.

The Court is aware, of course, that neither *Pogue* nor *Thompson* squarely addresses the issue of whether these kinds of false statements fall within §3729(a)(7)'s reach, presumably because the relators in those cases did not

advance that argument. The fact that neither the attorneys nor the courts even considered the possibility that section (a)(7) might apply is some indication of the novelty of relator's theory in this case. More significant, however, is the courts' reluctance to extend the FCA to these types of statements even when the usual prerequisite of an FCA suit – the presentation of a claim for payment to the government – was undisputedly present. The concern voiced by even those courts that permit such cases to proceed is that, by doing so, the FCA is being transformed into something it was not intended to be – namely, a vehicle for allowing either the United States or a private citizen to file a suit for money damages whenever someone falsely states to the government that some unlawful act did not occur. At least in the context of sections (a)(1) and (a)(2), the existence of a claim for payment is a limiting factor on the FCA's reach. That is not the case with section (a)(7), which does not depend upon the presentation of a claim for payment. Thus, if Congress intended any limitations at all on the extent to which the FCA captures false statements made to the government when no claim for payment is presented, such limitations may be found either by construing strictly certain statutory language, such as the word "obligation," – the *Prawer* court position which defendants espouse – or by finding that the language chosen by Congress, even if not strictly limited to a legal obligation owed to the government, was not intended to apply to each and every statement which might conceal from the government the existence of criminal or civil violations to which monetary penalties might attach. The Court makes this latter finding.

One of the concerns expressed by the *Thompson* court was that, by applying the FCA in situations where at least implicit misrepresentations are made to the government in connection with some claim for payment – even if the misrepresentation does not affect the timing or amount of the payment – the FCA would be turned into a vehicle for private enforcement of the underlying statute or regulation. In the context of the "direct claim" provisions of the FCA, even if a more expansive interpretation of the language in §3729(a)(7) were adopted, there would be some limit on the extent to which the FCA became such a vehicle because, in those situations, the party being sued would have submitted some type of claim for payment, thereby limiting the reach of the FCA to statutory violations committed by those who have a relationship with the government that involves both a payment of money from the government to the defendant and some procedure through which the claimant falsely represents to the government that it is in compliance with rules or regulations which are involved in that relationship.

On the other hand, if the "reverse false claims" language is also construed to cover garden variety statutory or regulatory violations, the limiting factor of the existence of a claim for payment would not be present, because the essence of the "reverse false claim" is that the defendant has *not* presented a claim for payment to the United States. Under the relator's argument, it would be sufficient to impose liability under §3729(a)(7) if there has been some type of document found that falsely represents, either explicitly or implicitly, that the person has committed no statutory or regulatory violation which might lead to the imposition of a penalty or fine.

This Court does not believe that Congress, by amending the False Claims Act in 1986, intended to convert that Act into an all-inclusive vehicle for the enforcement of any federal statute or government regulation by either the Department of Justice or by a private citizen whenever it can be found that some false statement has been made regarding conduct subject to monetary sanctions. In this day of pervasive government regulation of both public and private conduct, it is impossible even to estimate the number of times each day, each month, or each year that private citizens create or submit some type of document required by the government or subject to government review or the number of times that such a document, if not completely accurate, could lead to the filing of a False Claims Act case.

The discharge of pollutants scenario addressed in the *McGinnis* and *Pickens* cases is a good example of the potentially limitless reach of the FCA under relator's interpretation. How many industries are required to either file reports or keep logs relating to their compliance with environmental statutes? How many more maintain records which, while not required to be kept, nonetheless may be inspected from time to time by the government, either as part of a routine inspection, or in connection with some completely unrelated matter? Under *Pickens* and *McGinnis*, any entry in any business record of any business subject to the environmental laws of the United States which did not accurately report the unlawful discharge of a pollutant, the unlawful transportation of hazardous waste, or some other type of activity

which violated the environmental laws, could give rise to the filing of a False Claims Act case.[6]

Of course, the environmental laws are not the only pervasive regulations of the United States which apply to the everyday operation of businesses. For example, most businesses are also subject to the Occupational Safety and Health Act ("OSHA"), 29 U.S.C. §§651 *et seq.* 29 U.S.C. §654 imposes an obligation on each such employer to maintain a safe work place, and §657(c)(1) requires those employers to keep records about their compliance with OSHA. These records are subject to inspection both on a routine basis as part of OSHA's compliance monitoring function, and in connection with OSHA inspections or execution of search warrants made in response to a specific safety complaint. 29 U.S.C. §666(c) states that any violation of 29 U.S.C. §655 or any rule or regulation of OSHA can subject violators to fines ranging up to

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[6] This is not to say that a violation of the environmental laws or other laws may not be the predicate for a False Claims Act case. *In United States ex rel. Fallon v. Accudyne Corporation*, 880 F.Supp. 636 (W.D. Wis. 1995), the defendant allegedly made false statements and certifications that it had complied with environmental regulations required by its contract with the government in order to induce payments by the government under its contract. Such conduct may well fall within the prohibition against submitting a false claim under 31 U.S.C. §3729(a)(1) and (a)(2). Under relator's interpretation in the present case, it would not be necessary to show any contractual relationship with the government or receipt of any payment from the government; a violation of environmental regulations that could result in monetary sanctions, coupled with false records regarding compliance, would alone be sufficient to institute a False Claims Act case under §3729(a)(7), an interpretation that is not adopted by this Court.

$70,000. Was it Congress' intent that if an employer fails to keep accurate records of its compliance with OSHA, no matter how minor the failures might be, a private party who learns of this failure can bring a *qui tam* action under the False Claims Act because the failure to comply with OSHA or to keep accurate records may lead to the imposition of a civil penalty? There are, of course, countless other record-keeping requirements found in federal law – for example, those relating to the purchase and sale of firearms, the purchase and sale of narcotic drugs by pharmacists and pharmacy supply houses, the inspection of meat, poultry, and other food items under the Food, Drug and Cosmetic Act – in short, a myriad of laws and regulations which, in one way or another, regulate almost any significant business activity carried on in the United States. Congress and regulatory agencies have set forth specific sanctions for the violations of these laws and regulations, and the False Claims Act, in this Court's view, is not intended to be some super enforcement tool with a private right of action for the imposition of some new and additional penalty.

Another, even more extreme, example may illustrate the *Prawer* Court's concern that unless some narrowing construction is placed on §3729(a)(7), it will be as broad as a "lawyer's creative impulses" can make it, *see* 946 F.Supp. at 94-95 n. 13. 42 U.S.C. §1983 provides a civil remedy to persons whose constitutional rights are violated by one acting under color of law. Countless thousands of private actions are filed each year under this statute, many of them by state employees complaining about job actions or by state prisoners complaining about

actual or perceived abuses. Although §1983 does not provide for monetary penalties or fines running to the government, that statute has a criminal counterpart, 18 U.S.C. §242, which permits a fine to be levied against a person acting under color of law who deprives another person of constitutional rights. Other than the fact that §242 contains a scienter element (willfulness) not present in §1983, the language of the statutes is very similar – which is not surprising, since the predecessor of §1983 was one of three statutes which were consolidated into the predecessor of §242 in 1871. *See United States v. Lanier*, 73 F.3d 1380, 1385 (6th Cir. 1996) (en banc), *rev'd on other grounds* 117 S.Ct. 1219 (1997).

Most state employers and state prisons keep records of their employees' conduct, including conduct which can form the basis for a §1983 lawsuit. It is not unusual to find in these records a denial that any unlawful conduct occurred, or at least the absence of an indication that it did. It is also not unusual for some arm of the federal government, such as the EEOC, for example, or the Department of Justice to review such records.[7] Although such records may not be required to be kept or submitted, under relator's theory, and in accordance with the decision in *McGinnis*, "[t]he FCA . . . does not require that the

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[7] With certain exceptions, the enforcement of all federal statutes affecting civil rights, including those pertaining to elections and voting, public accommodations, public facilities, school desegregation, employment, housing, abortion, sterilization, credit and civil rights of Indians and institutionalized persons is assigned to the Assistant Attorney General, Civil Rights Division, Department of Justice. 28 C.F.R. §0.50.

false record be one that the defendant is under an obligation by law to maintain." 916 F.Supp. at 708. Taking this argument to its logical conclusion, in any instance where the government has reviewed any record dealing with the conduct about which a plaintiff complains, that §1983 plaintiff may properly allege that the defendant's "false" records (*i.e.* any record that does not acknowledge the commission of the underlying §1983 violation) "concealed" a violation of 18 U.S.C. §242 from the government, thereby depriving the government of the opportunity to collect a criminal fine, and violating the False Claims Act. Further, so long as the word "willful" is used in the complaint to describe the defendant's underlying conduct, the FCA claim presumably would survive a motion to dismiss. Is it reasonable to conclude that, by adopting §3729(a)(7), Congress intended that reverse false claims of this nature could be routinely pleaded in §1983 litigation?

The Court believes that the answer to these questions is obvious. So drastic an expansion in the scope of the False Claims Act, through the use of language which strongly implies that there be some type of financial relationship between the defendant and the United States which is subject to being affected by an act of concealment or avoidance, could not reasonably have been intended. The legislative history suggests nothing more than that Congress was concerned that in cases where a pre-existing obligation to the United States exists but is reduced or eliminated through the submission of some type of false statement, the government or a private citizen may redress the injury to the Treasury through the filing of a False Claims Act case.

The language Congress used and the legislative history simply cannot be reconciled with the recognition that literally millions of records are maintained by every business engaged in commerce within the United States; that a failure to maintain accurate records frequently subjects the business to sanctions under specific statutes and regulations; and that innumerable private lawsuits could be filed if the FCA is viewed as a tool to obtain a damage award for improper or inaccurate record keeping that fails to reflect some alleged violation of federal law. If that is what Congress intended, it should have plainly said so.

Yet another reason to doubt Congress' intention to create a private remedy based on the enforcement of an extensive number of statutory or regulatory requirements is the issue of damages. The FCA permits a private plaintiff to recover a percentage of the money otherwise due to the United States. In a case where the obligation which is being concealed arises from a contract or a debt, such as a judgment, calculating the amount of the award is relatively straightforward. In cases where the underlying "obligation" is a fine, penalty, or assessment, things are not as simple. Most statutes and regulations provide for a range of monetary penalties, and give government agencies substantial discretion concerning the amount of the penalty to be assessed. Criminal statutes, such as 18 U.S.C. §545, allow a sentencing judge to assess a fine within the statutory range, aided by the United States Sentencing Guidelines, when applicable. It is difficult to envision what procedure would be used in an FCA case to determine exactly what amount of money, in the form

of penalties or fines, the government would hypothetically be entitled to for violations of statutes or regulations which the government has chosen not to enforce directly against the defendant. Again, both the FCA and the legislative history are completely silent on how this issue might be addressed by a court which adopted the expansive interpretation of §3729(a)(7) sought by relator.

The Court sees no principled way to distinguish all of the examples given above from the facts of this case. The importation of goods into the United States is yet another example of an ordinary, everyday business activity which, because it is regulated by the United States, is accompanied by record keeping requirements which, unquestionably, can be violated and when violated subject the violator to specific statutory and regulatory sanctions. If the False Claims Act reaches these types of transactions, it also reaches every environmental law violation, OSHA violation, and any other regulatory violation which could be committed by a business, at least where the business keeps some record of that activity which is arguably false and which, at some point in time, is reviewed by the government. It is unnecessary in the present case for the Court to determine the precise contours of the language chosen by Congress to effectuate a "reverse false claims" remedy, and the proper definition of the term "obligation" may well go beyond that contemplated by the *Prawer* court to include matters other than direct contractual obligations or claims which have been reduced to judgment. It is sufficient in the present case for the Court to find, as it does, that the language of §3729(a)(7) is not so broad as to encompass every statutory or regulatory violation which might lead the United

States to attempt to assess a fine or other type of monetary penalty against the violator.

It might be argued, however, that Count Five of the complaint, which alleges concealment of an obligation (now found in 19 U.S.C. §1304(h)) to pay an additional ten percent *ad valorem* duty, stands on a different footing than the other counts. Relator appears to assert that the existence of the *ad valorem* duty described in this statute does not depend upon a government official's exercise of discretionary authority to levy or to pursue a criminal fine or civil penalty, but rather arises simply by operation of law. Relator further notes that, by the terms of the statute, this duty is "not [to] be construed to be penal" and "shall not be remitted in whole or in part nor shall payment thereof be avoidable for any cause." Thus, relator argues, the mere arrival of mismarked goods on a loading dock in the United States triggered the defendants' obligation to pay this duty, and the filing of false entry documents concealed its existence from the government and gave rise to liability under §3729(a)(7).

Although Count Five may present a closer question than do the other counts of the Complaint, in the Court's view it fails to state a claim under the False Claims Act.

It should first be noted that this is not a case in which a false statement is made to the Customs Service in order to avoid the payment of a duty which is due and owing to the government as, for example, the marking of goods with a country of origin having a lower duty than the country from which the goods actually originated. In that situation, there is clearly an existing obligation to pay the correct duty and, if not paid, the government has been

deprived of duties to which it is entitled. In the present case, defendants note that "the amount of the customs duties owed the United States was *not* affected by whether China, Macao or Hong Kong was designated as the country of origin," (Defendants, memorandum in support of motion to dismiss, p. 3), and this has not been disputed by relator. Instead, the alleged mismarking of the goods created, at best, a conditional obligation to pay money to the government in the future.

As the Federal Circuit has noted, a culpable mismarking of goods imported into this country can give rise to a violation of two statutes, 19 U.S.C. §1304(h) and 19 U.S.C. §1592(d). *Pentax Corporation v. Robison*, ___ F.3d ___, (Fed. Cir., Sept. 17, 1997), 1997 WL 573492. Section 1304(h) provides that if an article at the time of importation is not properly marked regarding the country of origin and *if* such article is not exported or destroyed or properly marked after importation, then – and only then – a duty of 10% *ad valorem* shall be levied, collected and paid. The act of importing such goods does not itself create "an obligation to pay or transmit money or property to the Government," *see* 31 U.S.C. §3729(a)(7). Rather, if, after importation, the goods are then exported, destroyed or properly marked, there is no obligation to pay the additional *ad valorem* duty. Even if not exported, destroyed or properly marked, there is no obligation to pay the additional *ad valorem* duty until such time as the Customs Service levies the additional duty. Only at that time is there an obligation "to pay or transmit money or property to the Government." False statements in the required customs documents regarding the country of origin are arguably statements made to avoid a *potential*

obligation to pay money to the government if certain events do or do not taken place, *i.e.* if exportation, destruction or correct marking does not occur and if the levy made by the Customs Service does occur, but it cannot be said that the false statements alone avoid a present obligation to pay money or property to the government.[8] In this sense, the additional *ad valorem* duty (although not deemed to be penal) is of the same nature as other civil or criminal penalties that potentially can be imposed for the violation of a host of federal statutes. While Congress clearly intended that a reverse false claim is actionable when false statements are made to conceal,

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[8] Relator concedes that Congress' use of the words "conceal" and "decrease" in 31 U.S.C. §3729(a)(7) can reasonably be construed to refer to present and existing obligations to the government, but contends that inclusion of the word "avoid" should be construed to apply to the possibility of future obligations (Opposition of Relator to Motion to Dismiss, p. 15). An existing obligation, however, could also be "avoided" by a false statement. For example, if a company has a contract to provide property to an agency of the government that excuses performance if certain events occur, and the company falsifies its records to show the occurrence of such an event, it seems to the Court that the company has not made a false statement to "conceal" the contractual obligation to perform the contract or to "decrease" that obligation, but has made the false statement to "avoid" its obligation to perform the contract. The point is that avoidance can be reasonably interpreted to include the avoidance of an existing obligation to the government and not just the avoidance of some potential future obligation. The Court finds no merit in relator's contention that Congress necessarily intended that the word "avoid" include all *in futuro*, inchoate obligations that conceivably could arise from a violation of some federal statute or regulation.

avoid or decrease an existing obligation to the government, the expansive, unlimited interpretation urged by relator would create a False Claims Act case whenever it could be shown that a violation of a statute *could* result in the imposition of some monetary sanction, and it would permit a private citizen to request, and a Court to impose, a monetary penalty above and beyond the specific sanction tailored by Congress to fit that offense.

19 U.S.C. §1592 is an illustration of the type of statute that Congress has enacted to address the penalties to be imposed for the specific misconduct alleged in this case. It prohibits the importation of any merchandise into the commerce of the United States by means of any false statement and provides for specific penalties, after notice and opportunity to be heard, which depend on whether the violation was the result of fraud, gross negligence or simple negligence. It also caps the maximum penalties if the importer discloses the violation before the commencement of a formal investigation of the violation. Under relator's interpretation of the False Claims Act, this carefully crafted statute providing specific penalties for a fraudulent statement in the importation of mismarked goods could be bypassed by a private citizen bringing an action under the reverse false claims provision of 31 U.S.C. §3729(a)(7). It would also serve to bypass the statutory requirement that in an action brought by the United States Attorney for the recovery of any fine, penalty or forfeiture based on fraud, the government has the burden of proof to establish the alleged violation by clear and convincing evidence, *see* 19 U.S.C. §1592(e)(2), as well as the five-year statute of limitations for bringing an

action to recover any duty, pecuniary penalty of forfeiture of property. 19 U.S.C. §1621.

Even though Count Five may stand on a somewhat different footing than relator's other claims, the Court is still persuaded that it does not come within the ambit of the reverse false claims provision of 31 U.S.C. §3729(a)(7).

IV.

Although the government declined to intervene in this action, the Department of Justice, through the United States Attorney for the Central District of California, filed an *amicus curiae* brief opposing defendants' motions to dismiss. That brief, however, was limited to only one of the issues raised by the motions to dismiss, *i.e.* whether the comprehensive administrative scheme of the customs laws provides for enforcement only by the Customs Service and precludes a private *qui tam* action under the False Claims Act.[9] Stating that "As the primary enforcer of the False Claims Act, the U.S. Department of Justice . . . has a significant interest in the proper resolution of issues bearing upon federal court jurisdiction over *qui tam* actions" (Amicus Curiae brief, p. 2), the Department opposed the argument of defendants that the customs

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[9] This is an issue the Court has not addressed in this opinion in light of the Court's finding that §3729(a)(7) does not encompass relator's claim. It is thus unnecessary to decide whether, if relator's claim fell within the proper scope of the False Claims Act, it would conflict with the alleged intent of Congress, in enacting a comprehensive regulatory scheme to deal with customs violations, to preempt any private cause of action predicated upon violations of the customs laws.

laws precluded a *qui tam* action but expressly took no position regarding the basic question of whether the relator has stated a claim upon which relief can be granted, stating:

> It may or may not be the case, as defendants have argued in other sections of their memoranda, that relator's allegations, even if true, fail to state a proper False Claims Act claim. [FN 6]
>
> [FN 6] The government does not intend to address that issue in this brief.

Amicus Curiae brief, p. 5.

After the case was transferred to this Court, the Department of Justice, through the United States Attorney for the Southern District of Ohio, filed a supplemental brief in which the Department not only reiterated its earlier argument but, for the first time, opposed defendants' argument that the *Prawer* court's definition of "obligation" is the one that should be adopted by this Court. (Supplemental Amicus, Curiae brief, pp. 3-8).

This Court, however, finds more persuasive the position taken by the Department of Justice in *United States ex rel. Sequoia Orange Co. v. Oxnard Lemon Co.*, Case Nos. CV-F-91-194, 195, 196 & 197 OWW, (E.D. Cal.), in which the Department, at some length, argued forcibly that §3729(a)(7) does not encompass a claim based on the submission of false records to avoid payment to the United States of forfeitures or fines.[10]

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[10] An unreported decision in that case, issued on May 4, 1992, appears at 1992 WL 795477. The government's argument

Although Congress appears to have originally intended to proscribe the submission of so-called reverse false claims, *see* S.Rep. 99-345 at 18-19, in order to eliminate any lingering uncertainty, the False Claims Amendments Act of 1986 included a provision expressly proscribing the submission of such claims. *See Smith v. United States*, 287 F.2d 299 (5th Cir. 1961); *United States v. Douglas*, 626 F.Supp. 621 (E.D. Va. 1985). Furthermore, both the Senate Report accompanying the 1986 amendments to the False Claims Act, and the congressional testimony of Department of Justice officials, demonstrate that the goal of the reverse false claim provision was to ensure that individuals seeking to avoid paying money "owed" the Government would be found equally liable under the Act as if they had submitted a false claim to receive federal funds. In introducing the Act's new provision covering reverse false claims, the Senate Report refers specifically to "fraudulent attempts to pay the Government less than is owed in connection with any goods, services, concessions or other benefits." S.Rep. No. 345 at 9.

This language is entirely consistent with the Government's argument that an attempt to circumvent an obligation to pay created solely as the result of a violation of an administrative enforcement statute does not constitute a cognizable claim under the Act. The civil forfeitures that could be imposed if Oxnard has, in fact,

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was rejected, and the court held that any false reports submitted by the defendants to the government in that case with the effect that payments of forfeitures or fines to the government were avoided constituted false claims under the reverse false claims provision of the False Claims Act, 31 U.S.C. §3729(a)(7).

> violated the prorate regulations, *see* Agricultural Marketing Agreement Act, 7 U.S.C. §608a(5), are anything but sums "owed" the Government in the sense presumably intended by Congress and strongly suggested by the relevant legislative history – *i.e.*, money owed the Government in connection with or in exchange for Government "goods," "services" or "benefits." In fact, Sequoia's theory would make *any* violation of *any* statute or regulation(s) that has a civil or criminal, penalty, a violation of the False Claims Act as well. [FN 4] (emphasis in original).

The government's language in footnote 4 is especially pertinent in this case. It reads, in part, as follows:

> Not every false statement or record submitted in connection with even a bona fide Government benefits program gives rise to liability under the Act; rather, only those fraudulent records and statements that: (1) seek to obtain more Government money or property than would otherwise be due; or (2) represent that the Government is owed less money or property than is actually the case, constitute actionable False Claims Act violations. False claims submitted by individuals or entities seeking to avoid payment to the Government of administrative fines, penalties or forfeitures (OSHA, FAA, SEC, etc.), or criminal fines imposed pursuant to Title 18 of the United States Code, are not the stuff of False Claims Act lawsuits, regardless of whether the fine or forfeiture, payment of which has been evaded, is imposed in connection with the violation of a federal benefits program.

United States ex rel. Sequoia Orange Company v. Oxnard Lemon Co., supra, Memorandum of the United States in support of its motion to dismiss, pp. 6-7, n.4.

In its reply to the relator's opposition to the government's motion to dismiss the complaint in the *Sequoia* case, the government reiterated, in the following language, its interpretation of the limited scope of the reverse false claim provision and expressed concern about the possible consequences of adopting the expansive interpretation advanced by the relator in that case, the same interpretation which the relator in this case urges upon the Court:

> There is a fundamental dispute between the government and the relator as to the scope and applicability of the False Claims Act. The government believes that the touchstone in determining whether the FCA applies to past conduct must be the identification of some *loss or potential loss to the Treasury through a false claim or statement submitted pursuant to a contract or agreement with the United States*. In relator's view, any false statement made in response to a federal regulatory requirement, where such false statement may be punished by a civil monetary penalty, should also be actionable under the FCA. *See* Opposition at 14-15. Relator's interpretation, which would authorize private parties to unilaterally use the FCA as an omnibus federal regulatory enforcement statute, finds no support in the Act itself or its legislative history. Moreover, it contains the potential (already realized to some extent in Sequoia's ongoing *qui tam* litigation against other orange handlers) for a for-profit entity to act in the guise of a private attorney general to harass its competitors and

> possibly to obtain an advantage in the marketplace thereby. (emphasis in original)

United States ex rel. Sequoia Orange Company, supra, Government's reply to relator's opposition to motion to dismiss, pp. 4-5. This Court agrees with the terse, but accurate, statement of the government in *Sequoia Orange* that, notwithstanding a relator's assertion that a defendant has engaged in patently unlawful conduct, "False claims submitted by individuals or entities seeking to avoid payment to the government of administrative fines, penalties or forfeitures (OSHA, FAA, SEC, etc.) or criminal fines imposed pursuant to Title 18 of the United States Code, are not the stuff of False Claims Act lawsuits. . . . "

V.

Despite the remedial purpose served by the False Claims Act, there are limits to a private party's ability to step into the shoes of the government and pursue an action against another party for allegedly violating a duty owed to the government. The Court believes that to recognize a cause of action in relator's favor under the False Claims Act in this case would, on the facts presented here, exceed those limits. Consequently, the Court concludes that the motion to dismiss is well taken, and it will dismiss the complaint for failure to state a claim upon which relief can be granted under 31 U.S.C. §3729(a)(7).

Based upon the foregoing, the defendants' motion to dismiss the complaint, filed pursuant to Fed. R. Civ. P. 12(b)(6) is GRANTED. All other pending motions are DENIED AS MOOT. This action is DISMISSED WITH

PREJUDICE. The Clerk is directed to enter a judgment in favor of the defendants.

/s/ John D. Holschuh
John D. Holschuh, Judge
United States District Court

IN THE UNITED STATES DISTRICT COURT
FOR THE SOUTHERN DISTRICT OF OHIO
EASTERN DIVISION

UNITED STATES OF AMERICA ex rel. AMERICAN TEXTILE MANUFACTURERS INSTITUTE, INC.,	:	**Case No. C2-97-776**
Relator,	:	
v.	:	
THE LIMITED, INC., et al.,	:	
Defendants.	:	

MEMORANDUM AND ORDER

(Filed Dec. 22, 1997)

On November 20, 1997, one week after I had filed an opinion and order granting defendants' motion to dismiss relator's complaint, relator filed a motion to disqualify me and to vacate the order of dismissal. The motion is based on the fact that I was personally represented by Attorney James Arnold in a proceeding in the Mayor's Court of Upper Arlington, Ohio in May of this year and that Mr. Arnold is a partner in the firm of Vorys, Sater, Seymour and Pease, counsel for some, but not all, of the defendants in this case. The sequence of events dealing with this representation and the court's involvement with this case is briefly set forth as follows:

As a result of an automobile accident which occurred on May 11, 1997, I entered a no contest plea on May 15, 1997 to a traffic offense in the Mayor's Court of Upper

Arlington, Ohio. I employed James Arnold of the Vorys, Sater, Seymour and Pease law firm to represent me in this matter. I instructed Mr. Arnold to handle the necessary formalities and informed him specifically that I did not want to be treated any differently than any other person faced with the same charge. Although the matter was competently handled by Mr. Arnold, it was handled in a routine manner, and I do not regard Mr. Arnold's services as being outstanding or resulting in some special treatment for which I should be grateful to Mr. Arnold or to the law firm with which he is associated. It is my belief that I received the same sentence for the offense that would be given to most first offenders, regardless of whether the charged person was represented by counsel or not. I received Mr. Arnold's statement for the services he rendered, and I paid this statement in full on June 24, 1997.

John C. Elam is an attorney whom I have known for many years. He is familiar with my career as a practicing attorney and as a judge and with my reputation in the community. He also is the former chair of this Court's Advisory Committee. Mr. Elam was at one time, but no longer is, the managing partner of Vorys, Sater, Seymour and Pease. He is still associated with that law firm. It is my understanding that he did accompany Mr. Arnold in a meeting with the City Prosecutor and he also made a brief statement on my behalf at my court appearance in addition to the statement made by Mr. Arnold. The statements of Mr. Arnold, Mr. Elam and my own statement to the court were all made publicly, in open court, and in the presence of the media.

As counsel for relator has been informed by the Upper Arlington City Prosecutor, the disposition of my case in the Mayor's Court "was handled by normal procedure and no special treatment was given." (Supplemental Declaration of Paul D. Cullen, Sr. in Support of Relator's Motion to Disqualify, p.2, par. 3).

Subsequent to the termination of the proceedings in the Mayor's Court, Mr. Arnold informed me that he had checked all of his pending cases and found that he had two cases which were on my docket which had been consolidated: *Graham v. American Cyanamid Company*, C2-94-423, and *Lundy v. American Cyanamid Company*, C2-94425. Because Mr. Arnold had represented me, I did not want to handle a case in which he was personally involved as the attorney for a party and, accordingly, on June 11, 1997 I entered an order recusing myself from these cases and directed the Clerk to reassign the cases to another judge through the customary blind draw.

Also subsequent to the termination of the proceedings in the Mayor's Court, I telephoned the Honorable James H. Jarvis, United States District Judge for the Eastern District of Tennessee and a member of the Judicial Conference Codes of Conduct Committee. From my previous experience as a member of the Committee, I was aware that members of the Committee can be contacted for their views on matters involving application of the Code of Conduct for United States Judges. While the views expressed by individual members are not deemed to be opinions of the Committee, they are helpful to the inquiring judge in determining what his or her appropriate conduct should be under the circumstances. I asked Judge Jarvis whether Mr. Arnold's representation of me

would require my recusal in cases in which the law firm of Vorys, Sater, Seymour and Pease appeared as counsel. The law firm is the largest law firm in Columbus, Ohio having over 200 members with offices also in Cleveland, Ohio, Cincinnati, Ohio and Washington, D.C. and represents a number of parties in my Court. Judge Jarvis did not express an opinion on behalf of the Committee, but his personal opinion was that I should not decide any matters involving the Vorys firm so long as I was being currently represented by Mr. Arnold, but that this representation would end upon the submission and payment of Mr. Arnold's statement for legal service, after which I would be under no obligation to recuse myself from cases in which Vorys, Sater had appeared as counsel.

As noted above, I paid Mr. Arnold for his services on June 24, 1997, and he has not represented me in connection with the traffic charge since that date. Neither Mr. Arnold nor any other member of the Vorys firm ever represented me prior to my employment of Mr. Arnold regarding the traffic charge, nor has any member of the firm represented me subsequent to the termination of that employment.

After the termination of my employment of Mr. Arnold, the case of *United States ex rel. American Textile Manufacturers Institute, Inc. v. The Limited, Inc., et al*, was transferred on June 30, 1997 from the Central District of California to the Southern District of Ohio. On July 9, 1997 the case was docketed in this Court, and under a blind draw assignment system was placed on my docket and the docket of Magistrate Judge Terence Kemp

Magistrate Judge Kemp conducted a status conference with counsel shortly after the case was docketed in this Court and concluded that a motion to dismiss which had been filed by all defendants should be promptly decided. For this reason Magistrate Judge Kemp, on his own initiative and without any request on my part, prepared a preliminary draft of a proposed Opinion and Order ruling on the pending motion to dismiss. His draft recommended that the motion be granted. I carefully examined the draft and the authorities cited, read the briefs of the parties, conducted my own legal research, as well as reading the cases cited by the parties, and agreed with Magistrate Judge Kemp that the defendants' motion was well taken and should be granted. Thereafter, I made revisions and additions to the draft and worked with Magistrate Judge Kemp to prepare an Opinion and Order in a final form that represented my own decision. I carefully addressed all of the issues in a completely objective manner, and I did so without regard to the parties or their attorneys. I did not begin to consider the merits of the motion to dismiss until, at the earliest, late September of 1997, or more than four months after Mr. Arnold's last services were rendered to me, and approximately three months after his representation of me formally ended. At no time did it occur either to me, or to Magistrate Judge Kemp, who was fully aware of Mr. Arnold's representation of me, that any of the parties to this case might reasonably be concerned that Mr. Arnold's brief representation of me would influence me in deciding the legal issues in this case on the merits or that under the circumstances outlined above there would be any appearance of impropriety in my doing so.

Following the filing of the Opinion and Order on November 13, 1997, I was informed by the Staff Counsel of the Judicial Conference Committee on Financial Disclosure that the law firm of Cullen and O'Connell, Washington, D.C., attorneys for the relator, had requested copies of my financial disclosure reports. The application for these copies was apparently made on or about November 19, 1997. Although this made me realize that relator's counsel was seeking, after the adverse decision had been rendered, to find some basis to challenge the decision by challenging my impartiality, it never occurred to me that counsel would pursue this course by resurrecting the prior representation by Mr. Arnold which had terminated prior to the time the case was randomly assigned to my docket. To the best of my knowledge, neither the Cullen law firm nor its local counsel made any effort to determine from me or anyone else whether the prior representation by Mr. Arnold had terminated before filing the motion to disqualify me. I was first informed of the filing of the motion to disqualify by my law clerk on Monday, December 1, 1997. Relator has also filed a separate motion to reconsider the November 13, 1997 decision on its merits.

28 U.S.C. § 455(a) requires a judge to recuse himself or herself "in any proceedings in which his impartiality might reasonably be questioned." The standard for recusal is an objective one, "whether [a] reasonable person knowing all the surrounding circumstances, would consider the judge to be impartial." *United States v. Hurst*, 951 F.2d 1490, 1503 (6th Cir. 1991), *cert. denied*, 504 U.S. 915 (1992).

Counsel for relator misstates the law when he claims there is a two year "rule" that requires recusal under § 455(a) during that period in any situation involving the appearance of a law firm that previously represented a judge. There is no such rule. In *Duke v. Pfizer, Inc.*, 668 F.Supp. 1031 (E.D. Mich. 1987), *aff'd*, 867 F.21 [sic] 611 (6th Cir. 1989), the case relied on by relator, it happened that two years had elapsed since the firm had represented the judge and he quite properly concluded that no reasonable person could question his impartiality after such a long period of time had elapsed, but he did not establish, nor has any other court established, a mandatory two year waiting period. In fact, as counsel for relator earlier acknowledged, there is no "bright line" test in such cases and each case depends on its facts and circumstances, citing the following passage from *In re Cargill, Inc.*, 66 F.3d 1256 (1st Cir. 1995) at 1269 (Campbell, J., dissenting; appendix to dissent):

> The proper standard for ascertaining whether a judge's impartiality might reasonably be questioned under § 455(a) is whether the charge of lack of impartiality is grounded on facts that would create a reasonable doubt, not in the mind of the judge, or even necessarily that of the litigant, but rather in the mind of the reasonable person. *See United States v. Cowden*, 545 F.2d 257, 265 (1st Cir. 1976), *cert. denied*, 430 U.S. 909, 97 S.Ct. 1181, 51 L.Ed.2d 585 (1977). Section 455 (a) requires a contextual, case-by-case analysis. It does not imply bright-line rule disqualifying any judge who ever has personal dealing with an attorney whose firm represents litigants before the same judge. The existing case law on the subject of judge-attorney dealings rests on

> exceedingly fact-specific judgments, with different outcomes in different situations.
>
> Relator's Reply Memorandum, pp. 5-6.

This is a correct statement of the law, and the "contextual, case-by-case" analysis belies any notion that recusal is mandatory simply because Mr. Arnold of the Vorys firm represented me in a matter within two years prior to this case being assigned to me.

I believe that a reasonable person with knowledge of the surrounding circumstances would consider my decision in this case to have been rendered impartially.

1. The brief representation in the Mayor's Court by Mr. Arnold was a matter of public record. It ended before I ever received this case on my docket. Neither Mr. Arnold nor Mr. Elam is counsel for any party in the present case.

2. I recused myself in any cases on my docket in which Mr. Arnold appeared as counsel.

3. I sought an opinion from a member of the Codes of Conduct Committee regarding the need for recusal in cases in which the Vorys firm appeared as counsel.

4. I received this case by a blind draw assignment and took no action in it until requested to do so by Magistrate Judge Kemp.

5. Magistrate Judge Kemp, on his own initiative and without any request or suggestion by me, prepared a draft opinion with the recommendation that defendant's motion to dismiss be granted. I was not aware of what the Magistrate Judge's conclusion would be until I received his draft opinion.

6. It was only after I had read the briefs of the parties and the applicable case law that I agreed with Magistrate Judge Kemp that, as a matter of law, defendant's motion to dismiss should be granted.

7. The decision involves a pure question of law and accepts as true for the purpose of deciding the motion all allegations of fact asserted by the relator.

I believe that a reasonable person, with knowledge of these facts, would conclude that the decision I rendered was rendered fairly and impartially. I am also aware, however, that many of the events that preceded my decision as outlined above were not known to relator when the motion to disqualify me was filed. That motion is based on a fact that is not in dispute, that I failed to disclose the prior representation of Mr. Arnold and to give the parties an opportunity to either object or not to object to my participation in this case. It is argued that Mr. Arnold's personal representation of me would create in the mind of a reasonable person doubt as to my impartiality. Although I do not believe that under the circumstances such a doubt would arise, I am always inclined to resolve any such question in favor of recusal. During my entire tenure on this bench, I have avoided any situation in which a party or an attorney has, for any reason, questioned my impartiality. I simply do not want any litigant to believe that a decision I am required to make could somehow be influenced by what the litigant perceives – even without foundation – to be a feeling of partiality on my part. I also believe that it is important that my decision on defendants' motion dismiss – involving as it does, a pure question of law – be reviewed by the

appellate court solely on the merits and without the encumbrance of any question concerning my recusal.

Although the timing of the motion, as well as its tone and content, are suggestive of interest not in recusal, but in avoiding the consequences of an adverse ruling, I am willing to credit relator's claim that it, and all of its counsel, including those who practice regularly in the Southern District of Ohio, were not aware of Mr. Arnold's representation of me, and that relator would have requested the reassignment of this case at an earlier date had it been aware of that fact. Therefore, I am exercising my discretion in favor of recusal for the reasons stated and in order to remove the question of recusal from this case and to expedite the proceedings toward a resolution on the merits of the important substantive issue involved in this case.

The decision filed on November 13, 1997 speaks for itself. It involved purely a question of law and assumed that all allegations of fact asserted by relator were true. It was my view, and remains my view, that relator's claims do not come within the scope of the False Claims Act and for this reason the defendants' motion had to be granted. That result would have been the same had only those defendants who are not represented by the Vorys law firm filed the motion.

Because of the importance of the issue concerning the interpretation of the False Claims Act, I anticipated that an appeal would be taken to the Sixth Circuit Court of Appeals and that the Court of Appeals would carefully review my decision and then affirm my judgment if I am correct in my view of the applicable law or reverse my

judgment if I am incorrect in that view. In either event, an important issue, not yet decided by the Supreme Court, would be resolved by our Circuit. It is an issue that should be decided or the merits and not encumbered by an issue involving my recusal.

Relator has requested that, assuming I grant its motion for recusal, I also vacate the decision embodied in the November 13, 1997 Opinion and Order citing in support of its request *Liljeberg v. Health Services Acquisition Corp.*, 486 U.S. 847 (1987). The present case, however, is markedly different from *Liljeberg*. In the *Liljeberg* case, a district judge, while a member of the board of trustees of Loyola University, tried, without a jury, a sharply contested lawsuit involving Liljeberg's right to a certificate of need to construct and operate a hospital. Liljeberg had negotiated with Loyola to purchase a large tract of land from the university, the university standing to benefit greatly if Liljeberg obtained a certificate of need. Of critical importance in the trial was Liljeberg's version of oral conversations that were disputed. The judge credited Liljeberg's testimony, and ruled in his favor. In finding that the judgment rendered by the district judge should be vacated, the Supreme Court noted "the obvious conflict of interest that resulted form [sic] having a University trustee preside over the trial", *Id.* at 866, and that the judge's failure to disqualify himself after discovering this conflict of interest constituted a violation of §455(b)(4) which disqualified a judge if he "knows that he, individually or as a fiduciary . . . has a financial interest in the subject matter in controversy or in a party to the proceeding, or any other interest that could be substantially affected by the outcome of the proceedings." *Id.* at 867.

In the present case, I have no conflict of interest. I have no financial interest whatsoever in any of the parties to this litigation, as relator presumably knows from an examination of my financial disclosure reports.

Also, the present case does not involve any trial in which I was called upon to judge the credibility of a party's testimony. The only ruling I have made in this case involves a pure question of law, and my decision is subject to *de novo* review by the appellate court.

As courts have noted, even when there has been a clear violation of § 455(a), (and, in my view, no such clear violation has occurred in this case) that violation does not always warrant setting aside a judge's prior rulings. *Harris v. Champion*, 15 F.3d 1538 (10th Cir. 1994); *In re School Asbestos Litigation*, 977 F.2d 764 (3d Cir. 1992); *In re Continental Airlines Corp.*, 901 F.2d 1259 (5th Cir. 1990). Applying the criteria used in these cases, there is no risk of injustice to the parties if my prior decision is not vacated. That decision involves a question of law that will be examined thoroughly by the court of appeals to determine whether it is a correct interpretation of the False Claims Act or whether it is an incorrect interpretation of that Act. It will be examined on the basis that all of the relator's claims regarding the alleged facts are true. Furthermore, other cases will not be affected by not vacating my prior decision. The recusal in this case was occasioned by my employment of an attorney for a very brief period of time in an isolated case in Mayor's Court, and the recusal is based upon my own practice to grant recusal requests when made and to expedite a review of my decision in this case on its merits. My recusal in a case in which I had no conflict of interest and which involved

a pure question of law subject to complete *de novo* review by the court of appeals is not the type of case in which the public's confidence in the judicial system could be questioned.

It is also very important to note that relator has filed a Motion to Alter or Amend Judgment under Fed. R.Civ. P. 59 (e) seeking a reconsideration of my decision on the merits. While I will not, of course, rule on that motion, the new judge assigned to this case could, in my view, treat this motion as one seeking a *de novo* review of my decision, without the restrictions that certain case law has seemingly imposed upon such motions. In fact, I respectfully request that the new judge, in the exercise of his or her discretion, consider the defendants' motion to dismiss *de novo* in ruling on defendants' Rule 59 (a) motion, with full authority to set aside my judgment if the assigned judge disagrees with the decision on which it is based.[1]

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[1] Defendants, in their response to the motion to vacate, cite the standard precept that a Rule 59 motion should not be used simply to revisit issues already raised and decided in the opinion to which the Rule 59 motion is directed. That is a rule of convenience and not a limitation on the Court's power. "The district court may grant a motion to alter or amend the judgment where it is necessary to correct manifest errors of law," *Brown v. Presbyterian Healthcare Services*, 101 F.3d 1324, 1332 (10th Cir. 1996), *cert. denied sub nom.*, ___ U.S. ___, 117 S.Ct. 1461 (1997), and when purely legal issues are determined in a Rule 59 proceeding, the Court of Appeals' review of the District Court's decision is not limited to correcting abuses of discretion, but is plenary. *Huff v. Metropolitan Life Ins. Co.*, 675 F.2d 119, 122, fn 5 (6th Cir. 1982); *see also, Federal Kemper Ins. Co. v. Rauscher*, 807 F.2d 345, 348-49 (3d Cir. 1986). Although finality is an important consideration when a judgment has been entered,

If the assigned judge reaches a conclusion contrary to mine, he or she can set aside the judgment I entered and proceed with the necessary steps toward reaching a final disposition of this case. If, on the other hand the assigned judge is of the same opinion regarding the law as I have set it forth, he or she can deny relator's motion, and relator will then be able to appeal the decision on the merits without any question concerning the impartiality of the judge from whose judgment the appeal would be taken. In this manner relator will obtain what it seeks, a *de novo* review of defendants' motion to dismiss by a district judge whose impartiality is not questioned by relator, and the decision, whatever it may be, can be appealed to the Court of Appeals solely on the merits.

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when the judgment is immediately and timely brought into question by a Rule 59 motion,the court's decision to revisit the issues covered in the judgment is appropriately guided by "the need to render just decisions. . . . " *Lavespere v. Niagara Mach. & Tool Works, Inc.*, 910 F.2d 167, 174 (5th Cir. 1990), *rehearing denied*, 920 F.2d 259, *cert. denied*, ___ U.S. ___, 114 S.Ct. 171 (1993). Thus, not only may a party properly invoke Rule 59 (e) to request a District Court to reconsider or correct errors of law, *Binkley Co. v. Eastern Tank, Inc.*, 831 F.2d 333, 336 n.4 (1st Cir. 1987), "Rule 59(e) . . . encompass[es] motions to amend that require reversal of the prior judgement." *National Metal Finishing Co. Inc. v. Barclaysamerican/Commercial, Inc.*, 899 F.2d 119, 124 (1st Cir. 1990). As aptly stated in *In re Cook*, 205 B.R. 617, 622 (Bankr. N.D. Ala. 1996):

> The motion to alter or amend results in "plenary review to all aspects of the Order to which the Motion is directed, without the movant's need of alleging anything but any sort of error on our part." *In re Campfire Shop Inc.*, 71 B.R. 521, 524 (Bankr. E.D. Pa. 1987).

Conclusion

Relator's motion for recusal is granted and the motion to vacate the decision and judgment previously entered is denied. I recuse myself from further proceedings in this case and hereby transfer this case and relator's Rule 59 (e) motion to the Honorable Walter Herbert Rice, Chief Judge of this District, for the purpose of assigning a new judge in accordance with this Memorandum and Order.

IT IS SO ORDERED.

/s/ John D. Holschuh
John D. Holschuh, Judge
United States District Court

ADDENDUM – Following the drafting of the above Memorandum and Order, the court received today a letter from counsel for defendants suggesting that the motion for recusal be referred to another judge and that I retain jurisdiction to decide the relator's motion to alter or amend judgment. This would not be consistent with my duty to rule on the motion for recusal in the first instance and if I recuse to not rule on defendants' motion to alter or amend the judgment. The suggestion was made as a result of anticipated objections to discovery requests in support of relator's motion for recusal. The court having granted relator's motion for recusal, the discovery requests and any objections thereto are moot.

UNITED STATES of America ex rel. AMERICAN TEXTILE MANUFACTURERS INSTITUTE INC., Plaintiffs,

v.

THE LIMITED, INC.; The Limited London-Paris-New York, Inc.; Limited Too, Inc.; Intimate Brands, Inc.; Victoria's Secret Stores, Inc.; Victoria's Secret Catalogue, Inc.; Cacique, Inc.; Express, Inc.; Lerner New York Inc.; Lane Bryant, Inc.; Henri Bendel, Inc.; Structure, Inc.; Abercrombie & Fitch, Inc. Mast Industries, Inc.; Tarrant Apparel Group, d/b/a Fashion Resource, Inc.; Gerard Guez; and Todd Kay, Defendants.

No. C2-97-776.

United States District Court,
S.D. Ohio,
Western Division.

May 20, 1998.

Ann Louise Lugbill, James Burdette Helmer, Jr., Helmer, Lugbill, Martins & Morgan, Cincinnati, OH, Paul D. Cullen, Sr., Cullen & O'Connell, Washington, DC, Robert C. Bonner, Gibson, Dunn & Crutcher, Los Angeles, CA, Joseph A. Black, Diana E. Stein, K. Michael O'Connell, Cullen & O'Connell, Washington, DC, for plaintiffs.

David Freeman Axelrod, James E. Phillips, Michael J. Canter, Robert Neal Webner, Vorys, Sater, Seymour & Pease, Columbus, OH, John T. Boese, Fried, Frank, Harris, Shriver & Jacobson, Washington, DC, for The Limited, Inc.

Michael Joseph Canter, Vorys, Sater, Seymour & Pease, Columbus, OH, John J. Quinn, Arnold & Porter,

Los Angeles, CA, John T. Boese, Fried, Frank, Harris, Schriver & Jacobson, Washington, DC, for The Limited London-Paris-New York, Inc.

David Freeman Axelrod, James E. Phillips, Michael J. Canter, Robert Neal Webner, Vorys, Sater, Seymour & Pease, Columbus, OH, John T. Boese, Fried, Frank, Harris, Shriver & Jacobson, Washington, DC, for Limited Too, Inc.

Michael Joseph Canter, Vorys, Sater, Seymour & Pease, Columbus, OH, John J. Quinn, Arnold & Porter, Los Angeles, CA, John T. Boese, Fried, Frank, Harris, Shriver & Jacobson, Washington, DC, for Intimate Brands, Inc., Victoria's Secret Catalogue, Inc., Victoria's Secret Stores, Inc., Cacique, Inc., Express, Inc., Lerner New York, Inc., Lane Bryant, Inc., Henri Bendel, Inc., Structure, Inc. and Mast Industries, Inc.

David Joseph Young, Squire, Sanders & Dempsey, Columbus, OH, for Tarrant Apparel Group and Gerard Guez.

David Joseph Young, Squire, Sanders & Dempsey, Columbus, OH, Marc P. Goodman, Ciema Lili Salem, Leonard D. Venger, Cameron A. Port, John F. Libby, Manatt, Phelps & Phillips, Los Angeles, CA, for Todd Kay.

James Evan Rattan, United States Attorney's Office, Columbus, OH, Philip A. Shaikun, U.S. Department of Justice, Civil Division, Washington, DC, for United States of America, amicus.

ORDER

BECKWITH, District Judge.

On September 25, 1996, Relator, American Textile Manufacturers Institute, Inc., filed this action, pursuant to the False Claims Act, alleging that Defendants knowingly have engaged in the practice of filing false statements with the United States Customs Service concerning the country of origin of their apparel imports. (Doc. No. 1). On June 02, 1997, Defendants filed motions to dismiss under FRCP 12(b)(6) for failure to state a claim. (Doc. Nos. 23, 25, 26, and 27). On November 13, 1997, Judge Holschuh, of the U.S. District Court for the Southern District of Ohio[1], granted that motion and dismissed this suit, with prejudice. (Doc. Nos. 126 and 127). On November 28, 1997, Relator filed a motion to disqualify Judge Holschuh and to vacate the order of dismissal. (Doc. No. 129). While determining that the motion to disqualify was not well-taken, Judge Holschuh chose to step aside, because of his usual practice with motions to recuse and the importance of expediting the proceedings. (Doc. No. 138 at 10-11, 14). He denied the motion to vacate. (Doc. No. 138). The Honorable Walter Rice, Chief Judge of this District, reassigned the case to this Court. (Doc. No. 142).

Relator has filed a motion to vacate Judge Holschuh's order dismissing the case, a motion to alter the judgment under FRCP 59(e), and a motion to amend the amended

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[1] Relator initially filed this case in the United States District Court for the Central District of California. Defendants filed a motion to transfer venue, and the court entered an order transferring the case to the Southern District of Ohio, Columbus Division. (Doc. Nos. 18 and 84).

complaint. (Doc. Nos. 144, 130, 145). For the reasons provided below, none of Relator's motions are well-taken and the Court hereby denies Relator's motion to vacate, motion to alter the judgment, and motion to amend the amended complaint.

I. FACTS[2]

Relator is a trade association of domestic textile and apparel manufacturers. Defendants consist of corporations and individuals who engage in the business of importing apparel. In sum, Relator's 73-page amended complaint alleges that Defendants contracted with overseas manufacturers to ship apparel to Defendants in the United States. (Doc. No. 8). Allegedly, Defendants knowingly permitted the manufacturers to misidentify the country of origin on the packages shipped to Defendants. For instance, the label on a box of goods manufactured in the People's Republic of China would identify Hong Kong as the country of origin. This mislabeling would allow Defendants to import goods in excess of quotas imposed by the United States government. In this case, the country of origin identified did not affect the duties owed and paid by Defendants. (Doc. No. 126 at 33). Relator alleges that Defendants then falsified entry documents so that United States Customs officials would not discover that the shipment had been mislabeled.

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[2] In his order dismissing this case, Judge Holschuh provided a more detailed explanation of the facts and claims. (Doc. No. 126 at 1-10). The Court elects not to re-state the facts in detail here but will provide the following summary.

To generalize, Relator contends that by allowing the mismarking of the packages, Defendants violated statutes and regulations under which the United States could assess fines and penalties. (*See* Doc. No. 126 at 6-10). Relator argues that these fines and penalties constitute obligations which Defendants owed the government. Thus, when Defendants falsified the entry documents, they attempted to avoid an obligation owed to the U.S. government. Consequently, Defendants are subject to liability under a section of the False Claims Act ("FCA"), 31 U.S.C. § 3729(a)(7).[3] With the authority provided in the qui tam provisions of the FCA, Relator is pursuing the government's FCA claim and, if successful, would share in the government's recovery. *See* 31 U.S.C. § 3730(b).

II. ANALYSIS

A. Motion to Vacate Judgment

Relator has filed a motion to vacate under FRCP 60(b)(1) and 60(b)(6). (Doc. No. 129). It asserts that vacatur is the only way to "eliminate the 'taint' created by the appearance of impropriety" and to ensure true de

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[3] 31 U.S.C. § 3729(a)(7) provides as follows:

(a) Liability for certain acts. – Any person who –

(7) knowingly makes, uses or causes to be made or used, a false record or statement to conceal, avoid, or decrease an obligation to pay or transmit money or property to the Government,

"is liable to the United States Government for a civil penalty of not less than $5,000 and not more than $10,000, plus three times the amount of damages which the Government sustains because of the act of that person . . . "

novo review of the merits of this case. (Doc. No. 144 at 4). According to Relator, Judge Holschuh should have vacated the order under Rule 60(b)(6) when he agreed to step aside, and vacatur also is available now under Rule 60(b)(1) because Judge Holschuh erred when he failed to vacate the Order upon Relator's initial request. (*Id.*)

Relator argues that the Court should vacate the judgment because the circumstances culminating in disqualification created an appearance of impropriety. (Doc. No. 144 at 4-5). The Supreme Court has considered the appropriateness of vacating a judgment under FRCP 60(b)(6) on the grounds that, subsequent to the final judgment, a violation of 28 U.S.C. § 455(a)[4] is discovered.[5] *Liljeberg v. Health Servs. Acquisition Corp.*, 486 U.S. 847, 858, 108 S.Ct. 2194, 2202, 100 L.Ed.2d 855 (1988). The Supreme Court instructed courts, faced with this issue, to consider: (1) the risk of injustice to the parties in the particular case, (2) the risk that the denial of relief would produce injustice in other cases, and (3) the risk of undermining the

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[4] 28 U.S.C. § 455(a) provides as follows:

> "Any justice, judge, or magistrate of the United State [sic] shall disqualify himself in any proceeding in which his impartiality might reasonably be questioned."

[5] Judge Holschuh did not find a violation of § 455(a). (Doc. No. 138 at 13). By applying the Liljeberg factors, the Court is not suggesting that a § 455(a) violation did occur.

The Court acknowledges Defendants' argument that voluntary recusal, after a finding that a § 455 violation did not occur, does not warrant vacatur. (*See* Doc. No. 148 at 8); *See Pashaian v. Eccelston Properties, Ltd.*, 88 F.3d 77, 84 (2d Cir.1996). However, the Court finds that the Liljeberg factors are helpful in disposing of Relator's motion.

public's confidence in the judicial process. *Id.* at 864, 108 S.Ct. at 2205. The Court cautioned that while FRCP 60(b)(6) provides courts with the authority to vacate judgments whenever appropriate to accomplish justice, a court should apply the rule only in " 'extraordinary circumstances.' " *Id.* at 863-64, 108 S.Ct. at 2204-05 (citations omitted). Applied to this case, the factors do not weigh in favor of vacatur.

1. Whether the parties will suffer injustice.

A denial of the motion to vacate will not cause the parties to suffer injustice. Judge Holschuh did not find that a violation of § 455 occurred. He stepped aside citing both his normal practice with motions to disqualify and the importance of an expeditious resolution of the case on its merits without the encumbrance of a question of impropriety. As a policy matter, the Court is reluctant to vacate a judgment by a district judge who has not been disqualified but has voluntarily stepped aside.

The basis of Relator's motion for disqualification was that Judge Holschuh retained James Arnold of the Vorys, Sater, Seymour and Pease law firm ("Vorys, Sater") for representation in a legal matter occurring in May and June of 1997. (Doc. No. 138 at 1-2). Counsel, other than Mr. Arnold, from Vorys, Sater represent Defendants in the present case. Mr. Arnold and Judge Holschuh terminated their attorney/client relationship before this case was transferred to the Southern District of Ohio and before it was assigned, by blind draw, to Judge Holschuh. (Doc. No. 138 at 2 and 5).

Subsequent to the termination of the proceedings for which Judge Holschuh retained Mr. Arnold, Judge Holschuh telephoned the Honorable James H. Jarvis, United States District Judge for the Eastern District of Tennessee and a member of the Judicial Conference Codes of Conduct Committee. (Doc. No. 138 at 3). Judge Holschuh knew that Committee members could be contacted concerning matters involving application of the Code of Conduct for United States Judges. (*Id.* at 3-4). Judge Jarvis expressed his personal opinion, not an opinion on behalf of the Committee, that Judge Holschuh should not decide any matters involving the law firm of Vorys, Sater so long as Mr. Arnold represented Judge Holschuh but that he would be under no obligation to recuse himself from cases in which Vorys, Sater appeared as counsel after the representation ended, i.e., when he tendered payment for legal services. (*Id.* at 4).

In a sworn declaration, Relator's counsel stated that Relator is not aware of any facts to support an allegation of actual bias or any act of impropriety by the judge. (Doc. No. 129; Cullen Declaration). Relator has failed to identify any illogical, unreasonable, or irrational statements or conclusions that indicate bias on behalf of Judge Holschuh.

Magistrate Kemp was assigned, by blind draw, to this case. On his own initiative, Magistrate Kemp independently prepared a proposed Opinion and Order ruling on the motion to dismiss and recommending dismissal of the case. (Doc. No. 138 at 5). Judge Holschuh then examined this draft, the briefs of the parties, and the authorities cited, and conducted his own research. (*Id.*). He reached the same conclusion as Magistrate Kemp and revised and

supplemented Magistrate Kemp's opinion. (Doc. 138 at 5).

This Court, in addressing Relator's FRCP 59(e) motion, has reviewed Judge Holschuh's order for clear error or manifest injustice.[6]

Considering the facts and circumstances surrounding the basis of the motion to disqualify, coupled with the quality of review that the parties have received, the Court finds that the parties will not suffer injustice if the Court does not vacate the judgment. If there is a concern for prejudice to the parties, that concern should be for prejudice to Defendants if the Court vacates the judgment, grants Relator's motion to amend the complaint, and forces the parties to invest more time and resources into rearguing the issues.

2.- Whether denial of this motion will produce injustice in other cases.

The Court is not convinced that denial will create injustice in other cases. In agreeing to step aside, Judge Holschuh stated that he did not believe that, under the circumstances, a doubt as to his impartiality would arise.

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[6] If the motion to dismiss is granted, the Sixth Circuit will review those issues of law de novo. *See In re School Asbestos Litigation*, 977 F.2d 764, 786 (3d Cir.1992) (stating that failure to disqualify and vacate a ruling may be harmless error when an appellate court will later review a ruling on a plenary basis); *In re Continental Airlines Corp.*, 901 F.2d 1259, (5th Cir.1990) (stating that the risk of injustice to the parties in allowing to stand a summary judgment ruling is usually slight because those rulings are subject to de novo review).

(Doc. No. 138 at 10). As stated above, Judge Holschuh removed himself for reasons unrelated to questions of impartiality. (*Id.*). This case will not offer precedent for future cases in which impropriety is established.

The Court's concern here is that granting this motion may convey the wrong message and produce injustice in other cases. From July through November this case progressed in Judge Holschuh's court and Relator failed to raise any question regarding impartiality. The parties and the court devoted considerable time and expense to this case. On November 13, the day the court issued the order dismissing the case, a legal assistant employed by Relator's counsel conducted a search for news articles concerning Judge Holschuh. (Doc. No. 129; Risinger Declaration). She learned of the traffic incident and alerted Mr. Cullen, one of Relator's attorneys, who directed her to call the court which presided over Judge Holschuh's case. (*Id.*). She learned that Mr. Arnold, a member of Vorys, Sater, had represented Judge Holschuh, and she communicated that information to Mr. Cullen. (*Id.*).[7] Relator's counsel requested and applied for copies

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[7] Mr. Cullen describes a slightly different version than Ms. Risinger. In a sworn declaration, Mr. Cullen states that at approximately 2:45 p.m. on November 13, 1997, he received a telephone call from Magistrate Kemp's office, informing Mr. Cullen of the ruling on the motion to dismiss. (Doc. No. 129). Mr. Cullen read a faxed copy and "was struck by a number of things which, in [his] subjective opinion, caused [him] to have concern with respect to the Court's objectivity and impartiality." (*Id.*). In his declaration, Mr. Cullen did not identify those "number of things" that caused him concern. (*Id.*). Mr. Cullen concluded that he needed to inquire into the relationship between Judge Holschuh and opposing counsel.

of Judge Holschuh's financial disclosure reports on November 19, 1997. (Doc. No. 138 at 6). Approximately two weeks after the disfavorable ruling, which disposed of the case, Relator moved to disqualify the Judge. In doing so, it has moved to vacate the ruling, alter or amend the judgment, and amend its complaint. In other words, Relator requests a complete second bite of the apple. The strategy employed by Relator is questionable at best, and the Court refuses to reward Relator or encourage this trend. Litigants have a duty to investigate and inform the court of any perceived biases before the court and the parties invest time and expense in a case. Relator has posited no reason for the failure to make a timely inquiry into Judge Holschuh's background.

3. Whether a denial of the motion to vacate will undermine the public's confidence in the judicial system.

Denying the FRCP 60(b) motion will not undermine the public's confidence in the judicial process. Judge Holschuh found no grounds for disqualification. Relator's counsel stated under oath that Relator was not aware of any facts supporting an allegation of bias or impropriety. (Doc. No. 129, Cullen Declaration). A member of the Judicial Conference Codes of Conduct Committee has expressed his opinion, as stated above, that Judge Holschuh would not be under an obligation to recuse. In

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(*Id.*). On November 14, Mr. Cullen instructed Ms. Risinger to call the Mayor's Court and determine the identity of the firm that represented Judge Holschuh in the traffic incident. (*Id.*).

addition, Magistrate Kemp and this Court have conducted independent analyses of the merits of the motion to dismiss. Therefore, this Court finds that denying the motion to vacate would not weaken the public's confidence in the judicial system.[8]

B. Motion to Amend or Alter Judgment

Relator has moved, pursuant to FRCP 59(e) to amend or alter the judgment. The court may amend or alter a judgment for one of three reasons: (1) intervening change in controlling law has occurred, (2) evidence not previously available has become available, or (3) it is necessary to correct clear error of law or prevent manifest injustice. *Helton v. ACS Group*, 964 F.Supp. 1175, 1182 (E.D.Tenn.1997); *Keweenaw Bay Indian Community v. United States*, 940 F.Supp. 1139, 1141 (W.D.Mich.1996), rev'd. on other grounds, 136 F.3d 469 (1998); *North River Ins. Co. v. CIGNA Reinsurance Co.*, 52 F.3d 1194, 1218 (3d Cir.1995). A motion to alter or reconsider a judgment is an extraordinary remedy and should be granted sparingly because of the interests in finality and conservation of scarce judicial resources.[9] *Sussman v. Salem, Saxon & Nielsen, P.A.*, 153

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[8] Yet, Relator argues that vacatur is necessary to preserve public confidence in the integrity of the legal system. (Doc. No. 144 at 12). The Court perceives Relator's concern for public confidence as less than genuine. Relator does not express concern about whether the public's confidence in the integrity of the system will suffer from the knowledge that counsel, after months of litigation, has moved to disqualify the judge immediately after a disfavorable ruling on a dispositive motion.

[9] FRCP 59(e) is not a means by which a party may re-litigate issues previously considered. *Keweenaw Bay Indian Community v.*

F.R.D. 689, 694 (D.C.Fla.1994) *Pennsylvania Ins. Guar. Ass'n. v. Trabosh*, 812 F.Supp. 522, 524 (D.C.Pa.1992).

In its motion, Relator fails to specify which of the three grounds for amending a judgment applies here. Because Relator does not discuss any intervening changes in the law or newly-discovered evidence, the Court assumes that Relator's position is that amendment is necessary to correct a clear error of law or to prevent manifest injustice.

Relator objects to Judge Holschuh's interpretation of 31 U.S.C. § 3729(a). (Doc. No. 130 at 2). Specifically, Relator challenges the interpretation of the term "obligation." (*Id.* at 2-3). Because Congress failed to define this term, Judge Holschuh, in his order, analyzed the legislative history and case law which led to the statute and the few judicial decisions which have directly or indirectly addressed the issue. (Doc. No. 126 at 16-17). Judge Holschuh concluded that Relator's reading was novel and that Congress did not intend that the statute "apply to each and every statement which might conceal from

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Michigan, 152 F.R.D. 562 (W.D.Mich.1992), *aff'd.*, 11 F.3d 1341; *EEOC v. Argent Indus., Inc.*, 746 F.Supp. 705, 706 (S.D.Ohio 1989). If the movant simply regurgitates arguments previously presented or presents arguments which originally could have been argued, then the movant's proper recourse is an appeal to the circuit court. *Dana Corp. v. United States*, 764 F.Supp. 482, 489 (N.D.Ohio 1991); *see Keweenaw Bay Indian Community*, 152 F.R.D. at 563. The Court acknowledges Defendants' assertion that Relator has simply regurgitated prior arguments. (Doc. No. 133 at 3). In its discretion, the Court will allow some latitude considering the fact that the judge hearing the original motion has stepped aside and requested that this Court review his judgment.

the government the existence of criminal or civil violations to which monetary penalties might attach." (Doc. No. 126 at 24-25).

Judge Holschuh then considered the implications of a reading as broad as that suggested by Relator. (Doc. No. 126 at 26-30). *See United States v. Wells*, 519 U.S. 482, 117 S.Ct. 921, 931, 137 L.Ed.2d 107 (1997) (referring to two cases in which the Supreme Court considered the possible implications of proposed statutory interpretations). Judge Holschuh stated that the statute, under Relator's interpretation, would authorize the Department of Justice or any private citizen to enforce federal statutes or government regulations when a false statement has been made regarding conduct subject to monetary sanctions. (Doc. No. 126 at 26). As a result, private citizens could enforce laws and regulations including OSHA, environmental laws, 42 U.S.C. § 1983, and laws regulating the sale and purchase of firearms, the purchase and sale of narcotic drugs by pharmacists and pharmacy supply houses, and the inspection of food items under the Food, Drug and Cosmetic Act. (Doc. No. 126 at 26-30). Judge Holschuh concluded that the statutory language and the legislative history could not be reconciled with the recognition (1) that businesses engaged in commerce within the United States maintain millions of records, (2) that a failure to maintain accurate records subjects the business to sanctions pursuant to statutes and regulations, and (3) that an infinite number of private lawsuits could be filed if private citizens could obtain a damage award for inaccurate records that fail to reflect an alleged violation of federal law. (Doc. No. 126 at 30).

The Eighth Circuit has issued an opinion, subsequent to Judge Holschuh's order, which may provide some guidance. In *United States v. Q International Courier, Inc.*, 131 F.3d 770 (8th Cir.1997), the defendants allegedly engaged in a practice in which they would ship bulk mail from the United States to Barbados for the purpose of mailing the letters individually back to the United States. *Id.* at 772. At the time, the U.S. Postal Service charge for domestic mail was 29 cents per ounce, while the Postal Service charged the Barbadian postal service as little as one-tenth of that amount for the same delivery of mail throughout the United States. *Id.* The United States, on behalf of the Postal Service, sued defendants on the grounds that they had violated the reverse claims provision of the FCA. *Id.* According to the government, the defendants owed an obligation to the United States for the full domestic postage, and the defendants attempted to reduce this obligation through fraudulent statements or records. *Id.* The district court granted summary judgment to the defendants holding that the government failed to establish that the defendants had an obligation to pay postage within the meaning of the FCA. *Id.*

The Eighth Circuit agreed, holding that whether the defendant's practice constituted a violation of some other law was a question for another day, but that, in this case, the United States had failed to demonstrate that any of the defendants owed an "obligation" to the government within the meaning of the FCA. *Id.* According to the Eighth Circuit, legislative history supports the interpretation that an "obligation" is a present duty to pay money or property that "must have been an obligation in the

nature of those that give rise to actions of debt at common law for money or things owed." *Id.* at 773. The court reasoned that the deliberate use of the indicative, past tense in the words "money owed" suggested that Congress intended the FCA to apply only to existing legal duties. *Id.* Citing, as support, the decision in *United States ex rel. S. Prawer & Co. v. Verrill & Dana*, 946 F.Supp. 87, 93-95 (D.Me.1996), the Eighth Circuit reasoned that if Congress had wished to include attempts to avoid potential fines or sanctions, it would have used language which reflected that. *Id.* at 773.

The court rejected the statutes cited by the government as establishing an obligation. *Id.* at 773-74. In particular, the court found that a statute that authorized the Postal Service to seek payment of a penalty not exceeding the total postage, created a potential penalty which, on its own, did not create a common-law debt. *Id.* at 774. "A debt, and thus an obligation under the meaning of the False Claims Act, must be for a fixed sum that is immediately due." *Id.* An obligation cannot be merely a potential liability. *Id.* at 773. The court noted that while the statutes and regulations cited by the government may support a judgment that the defendants engaged in illegal or fraudulent activity, those statutes and regulations did not create an obligation owed to the government. *Id.* The court rejected the proposition that the criminal penalties available for violating certain postal statutes were obligations, reasoning that the statutes were designed to punish one who violates the statute but were not designed to create an obligation to pay postage. *Id.* at 774. The government finally argued that the defendant owes postage because the mail was actually domestic rather

than international mail. *Id.* The court held that even if the mail was considered domestic, the government failed to successfully identify any source imposing a duty on the defendants to pay postage. *Id.*

As stated above, the Eighth Circuit cited, as support, the Prawer decision. In his order, Judge Holschuh also relied on Prawer, which Relator has contended is, at best, based on "highly suspect" reasoning. (Doc. No. 59 at 18-19 and Doc. No. 130 at 16-17). The Prawer decision called into doubt the *United States ex rel. Sequoia Orange Co. v. Oxnard Lemon Co.*, 1992 WL 795477 (E.D.Cal.), *United States ex rel. Stevens v. McGinnis, Inc.*, 1994 WL 799421 (S.D.Ohio) and *Pickens v. Kanawha River Towing*, 916 F.Supp. 702 (S.D.Ohio) decisions, which form the basis of Relator's argument. *Prawer*, 946 F.Supp. at 95 n. 13. The *Prawer* court criticized these three decisions for not adequately discussing why statutory or regulatory violations give rise to an immediate obligation prior to any judgment. *Id.* Unable to define the scope of reverse false claims cases as interpreted by Sequoia Orange, Stevens, and Pickens, the *Prawer* court predicted that the scope would be as broad as "any lawyer's creative impulses." *Id.*

The Prawer court engaged in a discussion aimed at determining the scope of viable claims. *Id.* at 93-95. In discussing the interpretation of the word "obligation", the court pointed out that legislative history twice referred to "money owed" as the type of obligation involved. *Id.* at 95 (citation omitted). And, according to the court, "[m]oney is not 'owed' without a specific contract remedy, a judgment or an acknowledgment of indebtedness." *Id.* at 95. Both the *Q International* decision

and the *Prawer* decision, cited, as support in the *Q International* opinion, support Judge Holschuh's order.

Relator argues in support of its FRCP 59(e) motion that liability for the payment of marking duties constitutes an obligation within the meaning of FCA, as alleged in Count V of its complaint. (Doc. No. 130 at 6). According to Relator, the marking statute and Customs regulations support the conclusion that marking duties accrue at the time of importation. (Doc. No. 130 at 6-7). Thus, the obligation to pay those duties arises at importation. (Doc. No. 130 at 7).

The parties have addressed this argument in their briefs in support of and in opposition to the motion to dismiss. Judge Holschuh adequately addressed this issue and concluded that an obligation to pay marking duties pursuant to § 1304(h) accrues only if the importer fails to take corrective action and Customs then proceeds to levy the duties. (Doc. 126 at 33-36). While *Pentax Corp. v. Robison*, 125 F.3d 1457 (Fed.Cir.1997), opin. amended on rehearing, 135 F.3d 760, does not directly address the same issues as the case at hand[10], parts of that opinion

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[10] In *Pentax*, 125 F.3d 1457, Customs accused *Pentax* of mismarking the country of origin in violation of 19 U.S.C. § 1304(a). In an attempt to mitigate penalties for violating § 1592(a), which prohibited mismarking resulting from fraud, gross negligence, or negligence, *Pentax* informed Customs of its violations. *Id.* at 1460. Section 1592(c)(4) serves to limit the penalties assessed, pursuant to §§ 1592(c)(1)-(3), against persons who disclose violations before or without knowledge of the commencement of a formal investigation of such violations. *Id.* at 1458-59. Because *Pentax* disclosed their violations, the monetary penalty to be assessed under § 1592 could not exceed

are instructive. In explaining its ruling, the court stated that the obligation to pay ad valorem duty assessed under § 1304(f) does not arise unless a mismarking occurs followed by the failure to export, destroy, or remark the articles in accordance with § 1304. *Id.* at 1463. This language supports the order dismissing the present case.

Relator argues that Count IV, which involves customs bonds, alleges an attempt to avoid an obligation. (Doc. No. 130 at 9). According to Relator, the conditions

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a prescribed percentage of the " 'lawful duties of which the United States is or may be deprived.' " *Id.* at 1459 (citing 19 U.S.C. § 1592(c)(4)). Customs argued that this lawful duty included the 10% ad valorem duty under § 1304. *Id.* at 1460. The issue before the court was "whether the ad valorem duties assessed pursuant to section 1304(f) [were] duties of which the government ha[d] been deprived 'as a result of a violation of' section 1592(a), 19 U.S.C. § 1592(d), thus making them duties that must be tendered by Pentax before it can qualify for prior disclosure treatment under 19 U.S.C. § 1592(c)(4)." *Id.* at 1460.

Ruling in favor of Customs, the Court of International Trade held that marking duties under 19 U.S.C. § 1304(f) constituted "lawful duties" subject to recovery under §§ 1592(c)(4) and (d). *Id.* at 1460. The Federal Circuit reversed the CIT and agreed with Pentax that "the government was not deprived of the § 1304(f) ad valorem duties 'as a result of the section 1592(a) violation,' as required by section 1592(d), because it is not the case that the section 1304(f) violation would not have occurred but for the section 1592(a) violation." *Id.* at 1463. In other words, the court determined that it could not say, as required by § 1592(d), that but for the § 1592(a) violation the § 1304(f) violation would not have occurred.

attached to the bond create a contractual obligation. (*Id.* at 9-10). Judge Holschuh adequately addressed this issue along with the other claims. If Defendants presented falsified entry documents to Customs officials an obligation was not immediately due, *i.e.*, an obligation equivalent to a common law debt was not due.

Relator argues that Judge Holschuh's concern that damages would be difficult to calculate is not a proper basis for dismissing this action. (Doc. No. 130 at 12-14). Relator misinterprets Judge Holschuh's order. The order did not state or even suggest that because damages would be difficult to compute the action should be dismissed. Judge Holschuh considered the issue of damages in the context of interpreting the FCA, or more specifically, in the context of determining whether Congress intended to include such regulatory violations in the FCA. (Doc. No. 126 at 31).

Judge Holschuh noted that it would be difficult for courts or juries to determine what fine, assessment, or penalty the government would have been entitled to had it pursued the regulatory or statutory violation. (*Id.*). This is because statutes and regulations often provide the government agency with a range within which to assess a penalty. (*Id.*). Thus, Judge Holschuh concluded that if Congress had intended for the FCA to cover such statutory and regulatory violations, Congress likely would have addressed the issue of how damages would be determined. (*Id.*). However, neither the FCA nor the legislative history addresses this issue. (*Id.*).

For the reasons provided above, the Court finds that amendment of the order dismissing Relator's action is not

necessary to prevent clear error of law or manifest injustice.[11]

C. Motion to Amend the Complaint

On January 8, 1998, Relator moved, pursuant to FRCP 15, to amend its complaint. Relator states that it seeks leave to amend for the purposes of clarifying the existing claims, providing this Court with a "clean slate," and eliminating any "taint" of an appearance of impropriety following the disqualification. (Doc. No. 145 at 1-2 and 4-5).

Rule 15(a) provides that leave to amend " 'shall be freely given when justice so requires.' " *Foman v. Davis*, 371 U.S. 178, 182, 83 S.Ct. 227, 230, 9 L.Ed.2d 222 (1962). In general, the Sixth Circuit is "very liberal" in permitting amendments. *Northwestern Nat'l Ins. Co. of Milwaukee v. Joslyn*, 53 F.3d 331, 1995 WL 270995 *6 (6th Cir.1995). Certain factors, such as undue delay, bad faith, or dilatory motive on the part of the movant, repeated failure to cure deficiencies by amendments previously allowed, undue prejudice to the opposing party by virtue of allowance of the amendment, and futility of amendment, may warrant the denial of a motion to amend. *Id.*; *Foman*, 371 U.S. at 182, 83 S.Ct. at 230. The grant or denial of a motion to amend is within the discretion of the district

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[11] In the order in which Judge Holschuh volunteered to remove himself from this case, he requested that this Court treat this as a de novo review without the restrictions imposed, by case law, on FRCP 59(e) motions. (Doc. No. 138 at 14). Relator is not entitled to a de novo review. However, the Court has reviewed the decision de novo and finds no error.

court. *Id.* "[P]iecemeal litigation should be discouraged, not only because it is antagonistic to the goals of public policy, but also because it is prejudicial to the rights of individual litigants." *Troxel Mfg. Co. v. Schwinn Bicycle Co.*, 489 F.2d 968, 970 (6th Cir.1973), *cert. denied*, 416 U.S. 939, 94 S.Ct. 1942, 40 L.Ed.2d 290 (1974).

Relator's argument for amendment is not well-taken. Relator will not be denied an opportunity to argue its case on the merits if this motion is denied. Relator admitted that the proposed amended complaint only clarified existing claims. As admitted by Relator, the parties have filed over 1,000 pages of briefs and documents; certainly Relator has enjoyed many opportunities to clarify the claims and exhaust any issues. (Doc. No. 145 at 2). In its memoranda filed in support of the motions to vacate and to alter the judgment, Relator regurgitates many, if not all, of its earlier arguments. This further illustrates the fact that amending the complaint and starting over would be futile as Relator likely would assert the same claims and the same arguments. *See Marx v. Centran Corp.*, 747 F.2d 1536, 1550 (citing *Foman*, 371 U.S. at 182, 83 S.Ct. at 230). The Court fails to see the need for amendment.

Furthermore, the Court finds compelling reasons to deny leave to amend. Relator has exhibited undue delay, and perhaps, bad faith, in bringing this motion. Defendants filed their motions to dismiss on June 2, 1997. (Doc. Nos. 23, 25, 26, and 27). Defendants' supporting memoranda and later replies and supplemental memoranda, should have alerted Relator to the alleged deficiencies in its complaint. Relator admits that its proposed second amended complaint focuses more precisely on problems raised by Defendants in earlier briefs. (Doc. No. 145 at 2).

Judge Holschuh did not issue his order until November 13, 1997. (Doc. No. 126). Relator had several months to file a motion to amend their complaint, but rather waited until after the court granted Defendants' motion. *See Joslyn*, 1995 WL 270995 *6 (affirming district court's denial of motion to amend and noting that the movant had several months to seek leave to amend prior to the court's ruling); *Harris v. City of Auburn*, 27 F.3d 1284, 1287 (7th Cir.1994) (citation omitted) (stating that presumption that leave to amend is to be freely given disappears after judgment has been entered and, at that point, the movant must provide good reason to grant the motion). An open request for the Court to permit amendment to cure deficiencies, once the Court identifies those deficiencies, will not defeat a meritorious motion to dismiss pursuant to Rule 12(b)(6). Had Relator filed a motion to amend the complaint prior to the consideration of the motion to dismiss and accompanied that motion with a memorandum identifying the proposed amendments perhaps Judge Holschuh would have considered the motion to dismiss in light of the proposed amendments to the complaint and would not have dismissed this action had he been convinced that the proposed amendments would have cured the deficiencies in the complaint. Absent such a motion, however, Defendants were entitled to a review of the complaint as filed pursuant to Rule 12(b)(6). Relator is not entitled to an advisory opinion from the Court informing them of the deficiencies of the complaint and then an opportunity to cure those deficiencies.

Relator contends that granting amendment will benefit the Court by simplifying the case and promoting judicial economy. The parties have prepared and filed several

hundred pages of briefs related to Defendants' motions to dismiss. Magistrate Kemp and Judge Holschuh devoted the time and resources necessary to carefully review the briefs, research and analyze the issues, and draft an order. After that order was issued, Relator filed a motion to vacate, a motion to alter the judgment, and a motion to amend the complaint. Again the parties have prepared and filed several hundred pages of briefs and supplements related to these motions. This Court, in ruling on these motions has revisited the issues addressed in the order of dismissal. Now, Relator proposes that, in the interest of judicial economy, we start over with a new pleading and a new set of briefs. (Doc. No. 145 at 4).

Granting leave to amend would be futile as Relator proposes no new claims and has exhausted the issues relevant to the motion to dismiss in briefs to the court. Granting leave to amend also is not proper here because of Relator's undue delay and arguable bad faith in filing this motion.

III. CONCLUSION

For the reasons provided above, the motion to vacate is DENIED; the motion to alter the judgment is DENIED; and the motion for leave to amend is DENIED.

IT IS SO ORDERED.

98-3889

UNITED STATES COURT OF APPEALS
FOR THE SIXTH CIRCUIT

AMERICAN TEXTILE MANUFACTURERS INSTITUTE, INC.,	)	ORDER
Plaintiff-Appellant,	)	(Filed Nov. 2, 1999)
v.	)	
THE LIMITED, INC., ET AL.,	)	
Defendants-Appellees.	)	

BEFORE: KEITH, BOGGS, and CLAY, Circuit Judges.

The court having received a petition for rehearing en banc, and the petition having been circulated not only to the original panel members but also to all other active* judges of this court, and no judge of this court having requested a vote on the suggestion for rehearing en banc, the petition for rehearing has been referred to the original panel.

The panel has further reviewed the petition for rehearing and concludes that the issues raised in the petition were fully considered upon the original submission and decision of the case. Accordingly, the petition is denied.

ENTERED BY ORDER OF THE COURT

/s/ Leonard Green
Leonard Green, Clerk

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* Judges Nelson and Moore recused themselves from participation in this ruling.

31 U.S.C. § 3729. False claims

(a) Liability for Certain Acts. – Any person who –

(1) knowingly presents, or causes to be presented, to an officer or employee of the United States Government or a member of the Armed Forces of the United States a false or fraudulent claim for payment or approval;

(2) knowingly makes, uses, or causes to be made or used, a false record or statement to get a false or fraudulent claim paid or approved by the Government;

(3) conspires to defraud the Government by getting a false or fraudulent claim allowed or paid;

(4) has possession, custody, or control of property or money used, or to be used, by the Government and, intending to defraud the Government or willfully to conceal the property, delivers, or causes to be delivered, less property than the amount for which the person receives a certificate or receipt;

(5) authorized to make or deliver a document certifying receipt of property used, or to be used, by the Government and, intending to defraud the Government, makes or delivers the receipt without completely knowing that the information on the receipt is true;

(6) knowingly buys, or receives as a pledge of an obligation or debt, public property from an officer or employee of the Government, or a member of the Armed Forces, who lawfully may not sell or pledge the property; or

(7) knowingly makes, uses, or causes to be made or used, a false record or statement to conceal, avoid, or decrease an obligation to pay or transmit money or property to the Government,

is liable to the United States Government for a civil penalty of not less than $5,000 and not more than $10,000, plus 3 times the amount of damages which the Government sustains because of the act of that person, except that if the court finds that –

(A) the person committing the violation of this subsection furnished officials of the United States responsible for investigating false claims violations with all information known to such person about the violation within 30 days after the date on which the defendant first obtained the information;

(B) such person fully cooperated with any Government investigation of such violation; and

(C) at the time such person furnished the United States with the information about the violation, no criminal prosecution, civil action, or administrative action had commenced under this title with respect to such violation, and the person did not have actual knowledge of the existence of an investigation into such violation;

the court may assess not less than 2 times the amount of damages which the Government sustains because of the act of the person. A person violating this subsection shall also be liable to the United States Government for the costs of a civil action brought to recover any such penalty or damages.

(b) Knowing and Knowingly Defined. – For purposes of this section, the terms "knowing" and

"knowingly" mean that a person, with respect to information –

(1) has actual knowledge of the information;

(2) acts in deliberate ignorance of the truth or falsity of the information; or

(3) acts in reckless disregard of the truth or falsity of the information,

and no proof of specific intent to defraud is required.

(c) Claim Defined. – For purposes of this section, "claim" includes any request or demand, whether under a contract or otherwise, for money or property which is made to a contractor, grantee, or other recipient if the United States Government provides any portion of the money or property which is requested or demanded, or if the Government will reimburse such contractor, grantee, or other recipient for any portion of the money or property which is requested or demanded.

(d) Exemption From Disclosure. – Any information furnished pursuant to subparagraphs (A) through (C) of subsection (a) shall be exempt from disclosure under section 552 of title 5.

(e) Exclusion. – This section does not apply to claims, records, or statements made under the Internal Revenue Code of 1986.

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31 U.S.C. § 3730. Civil actions for false claims

(a) **Responsibilities of the Attorney General.** – The Attorney General diligently shall investigate a violation under section 3729. If the Attorney General finds that a

person has violated or is violating section 3729, the Attorney General may bring a civil action under this section against the person.

(b) Actions by Private Persons. – (1) A person may bring a civil action for a violation of section 3729 for the person and for the United States Government. The action shall be brought in the name of the Government. The action may be dismissed only if the court and the Attorney General give written consent to the dismissal and their reasons for consenting.

(2) A copy of the complaint and written disclosure of substantially all material evidence and information the person possesses shall be served on the Government pursuant to Rule 4(d)(4) of the Federal Rules of Civil Procedure.[FN1] The complaint shall be filed in camera, shall remain under seal for at least 60 days, and shall not be served on the defendant until the court so orders. The Government may elect to intervene and proceed with the action within 60 days after it receives both the complaint and the material evidence and information.

(3) The Government may, for good cause shown, move the court for extensions of the time during which the complaint remains under seal under paragraph (2). Any such motions may be supported by affidavits or other submissions in camera. The defendant shall not be required to respond to any complaint filed under this section until 20 days after the complaint is unsealed and served upon the defendant pursuant to Rule 4 of the Federal Rules of Civil Procedure.

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[1] See, now, Rule 4(i) of the Federal Rules of Civil Procedure.

(4) Before the expiration of the 60-day period or any extensions obtained under paragraph (3), the Government shall –

(A) proceed with the action, in which case the action shall be conducted by the Government; or

(B) notify the court that it declines to take over the action, in which case the person bringing the action shall have the right to conduct the action.

(5) When a person brings an action under this subsection, no person other than the Government may intervene or bring a related action based on the facts underlying the pending action.

(c) Rights of the Parties to Qui Tam Actions. – (1) If the Government proceeds with the action, it shall have the primary responsibility for prosecuting the action, and shall not be bound by an act of the person bringing the action. Such person shall have the right to continue as a party to the action, subject to the limitations set forth in paragraph (2).

(2)(A) The Government may dismiss the action notwithstanding the objections of the person initiating the action if the person has been notified by the Government of the filing of the motion and the court has provided the person with an opportunity for a hearing on the motion.

(B) The Government may settle the action with the defendant notwithstanding the objections of the person initiating the action if the court determines, after a hearing, that the proposed settlement is fair, adequate, and reasonable under all the circumstances. Upon a

showing of good cause, such hearing may be held in camera.

(C) Upon a showing by the Government that unrestricted participation during the course of the litigation by the person initiating the action would interfere with or unduly delay the Government's prosecution of the case, or would be repetitious, irrelevant, or for purposes of harassment, the court may, in its discretion, impose limitations on the person's participation, such as –

(i) limiting the number of witnesses the person may call;

(ii) limiting the length of the testimony of such witnesses;

(iii) limiting the person's cross-examination of witnesses; or

(iv) otherwise limiting the participation by the person in the litigation.

(D) Upon a showing by the defendant that unrestricted participation during the course of the litigation by the person initiating the action would be for purposes of harassment or would cause the defendant undue burden or unnecessary expense, the court may limit the participation by the person in the litigation.

(3) If the Government elects not to proceed with the action, the person who initiated the action shall have the right to conduct the action. If the Government so requests, it shall be served with copies of all pleadings filed in the action and shall be supplied with copies of all deposition transcripts (at the Government's expense).

When a person proceeds with the action, the court, without limiting the status and rights of the person initiating the action, may nevertheless permit the Government to intervene at a later date upon a showing of good cause.

(4) Whether or not the Government proceeds with the action, upon a showing by the Government that certain actions of discovery by the person initiating the action would interfere with the Government's investigation or prosecution of a criminal or civil matter arising out of the same facts, the court may stay such discovery for a period of not more than 60 days. Such a showing shall be conducted in camera. The court may extend the 60-day period upon a further showing in camera that the Government has pursued the criminal or civil investigation or proceedings with reasonable diligence and any proposed discovery in the civil action will interfere with the ongoing criminal or civil investigation or proceedings.

(5) Notwithstanding subsection (b), the Government may elect to pursue its claim through any alternate remedy available to the Government, including any administrative proceeding to determine a civil money penalty. If any such alternate remedy is pursued in another proceeding, the person initiating the action shall have the same rights in such proceeding as such person would have had if the action had continued under this section. Any finding of fact or conclusion of law made in such other proceeding that has become final shall be conclusive on all parties to an action under this section. For purposes of the preceding sentence, a finding or conclusion is final if it has been finally determined on appeal to the appropriate court of the United States, if all

time for filing such an appeal with respect to the finding or conclusion has expired, or if the finding or conclusion is not subject to judicial review.

(d) Award to Qui Tam Plaintiff. – (1) If the Government proceeds with an action brought by a person under subsection (b), such person shall, subject to the second sentence of this paragraph, receive at least 15 percent but not more than 25 percent of the proceeds of the action or settlement of the claim, depending upon the extent to which the person substantially contributed to the prosecution of the action. Where the action is one which the court finds to be based primarily on disclosures of specific information (other than information provided by the person bringing the action) relating to allegations or transactions in a criminal, civil, or administrative hearing, in a congressional, administrative, or Government Accounting Office report, hearing, audit, or investigation, or from the news media, the court may award such sums as it considers appropriate, but in no case more than 10 percent of the proceeds, taking into account the significance of the information and the role of the person bringing the action in advancing the case to litigation. Any payment to a person under the first or second sentence of this paragraph shall be made from the proceeds. Any such person shall also receive an amount for reasonable expenses which the court finds to have been necessarily incurred, plus reasonable attorneys' fees and costs. All such expenses, fees, and costs shall be awarded against the defendant.

(2) If the Government does not proceed with an action under this section, the person bringing the action or settling the claim shall receive an amount which the

court decides is reasonable for collecting the civil penalty and damages. The amount shall be not less than 25 percent and not more than 30 percent of the proceeds of the action or settlement and shall be paid out of such proceeds. Such person shall also receive an amount for reasonable expenses which the court finds to have been necessarily incurred, plus reasonable attorneys' fees and costs. All such expenses, fees, and costs shall be awarded against the defendant.

(3) Whether or not the Government proceeds with the action, if the court finds that the action was brought by a person who planned and initiated the violation of section 3729 upon which the action was brought, then the court may, to the extent the court considers appropriate, reduce the share of the proceeds of the action which the person would otherwise receive under paragraph (1) or (2) of this subsection, taking into account the role of that person in advancing the case to litigation and any relevant circumstances pertaining to the violation. If the person bringing the action is convicted of criminal conduct arising from his or her role in the violation of section 3729, that person shall be dismissed from the civil action and shall not receive any share of the proceeds of the action. Such dismissal shall not prejudice the right of the United States to continue the action, represented by the Department of Justice.

(4) If the Government does not proceed with the action and the person bringing the action conducts the action, the court may award to the defendant its reasonable attorneys' fees and expenses if the defendant prevails in the action and the court finds that the claim of the person bringing the action was clearly frivolous, clearly

vexatious, or brought primarily for purposes of harassment.

(e) Certain Actions Barred. – (1) No court shall have jurisdiction over an action brought by a former or present member of the armed forces under subsection (b) of this section against a member of the armed forces arising out of such person's service in the armed forces.

(2)(A) No court shall have jurisdiction over an action brought under subsection (b) against a Member of Congress, a member of the judiciary, or a senior executive branch official if the action is based on evidence or information known to the Government when the action was brought.

(B) For purposes of this paragraph, "senior executive branch official" means any officer or employee listed in paragraphs (1) through (8) of section 101(f) of the Ethics in Government Act of 1978 (5 U.S.C.App.).

(3) In no event may a person bring an action under subsection (b) which is based upon allegations or transactions which are the subject of a civil suit or an administrative civil money penalty proceeding in which the Government is already a party.

(4)(A) No court shall have jurisdiction over an action under this section based upon the public disclosure of allegations or transactions in a criminal, civil, or administrative hearing, in a congressional, administrative, or Government Accounting Office report, hearing, audit, or investigation, or from the news media, unless the action is brought by the Attorney General or the

person bringing the action is an original source of the information.

(B) For purposes of this paragraph, "original source" means an individual who has direct and independent knowledge of the information on which the allegations are based and has voluntarily provided the information to the Government before filing an action under this section which is based on the information.

(f) Government Not Liable for Certain Expenses. – The Government is not liable for expenses which a person incurs in bringing an action under this section.

(g) Fees and Expenses to Prevailing Defendant. – In civil actions brought under this section by the United States, the provisions of section 2412(d) of title 28 shall apply.

(h) Any employee who is discharged, demoted, suspended, threatened, harassed, or in any other manner discriminated against in the terms and conditions of employment by his or her employer because of lawful acts done by the employee on behalf of the employee or others in furtherance of an action under this section, including investigation for, initiation of, testimony for, or assistance in an action filed or to be filed under this section, shall be entitled to all relief necessary to make the employee whole. Such relief shall include reinstatement with the same seniority status such employee would have had but for the discrimination, 2 times the amount of back pay, interest on the back pay, and compensation for any special damages sustained as a result of the discrimination, including litigation costs and reasonable attorneys' fees. An employee may bring an action in

the appropriate district court of the United States for the relief provided in this subsection.

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18 U.S.C. § 545. Smuggling goods into the United States

Whoever knowingly and willfully, with intent to defraud the United States, smuggles, or clandestinely introduces or attempts to smuggle or clandestinely introduce into the United States any merchandise which should have been invoiced, or makes out or passes, or attempts to pass, through the customhouse any false, forged, or fraudulent invoice, or other document or paper; or

Whoever fraudulently or knowingly imports or brings into the United States, any merchandise contrary to law, or receives, conceals, buys, sells, or in any manner facilitates the transportation, concealment, or sale of such merchandise after importation, knowing the same to have been imported or brought into the United States contrary to law –

Shall be fined under this title or imprisoned not more than five years, or both.

Proof of defendant's possession of such goods, unless explained to the satisfaction of the jury, shall be deemed evidence sufficient to authorize conviction for violation of this section.

Merchandise introduced into the United States in violation of this section, or the value thereof, to be recovered from any person described in the first or second paragraph of this section, shall be forfeited to the United States.

The term "United States", as used in this section, shall not include the Virgin Islands, American Samoa, Wake Island, Midway Islands, Kingman Reef, Johnston Island, or Guam.

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19 U.S.C. § 1595a. Forfeitures and other penalties

(a) Importation, removal, etc. contrary to laws of United States

Except as specified in subsection (b) or (c) of section 1594 of this title, every vessel, vehicle, animal, aircraft, or other thing used in, to aid in, or to facilitate, by obtaining information or in any other way, the importation, bringing in, unlading, landing, removal, concealing, harboring, or subsequent transportation of any article which is being or has been introduced, or attempted to be introduced, into the United States contrary to law, whether upon such vessel, vehicle, animal, aircraft or other thing or otherwise, may be seized and forfeited together with its tackle, apparel, furniture, harness, or equipment.

(b) Penalty for aiding unlawful importation

Every person who directs, assists financially or otherwise, or is in any way concerned in any unlawful activity

mentioned in the preceding subsection shall be liable to a penalty equal to the value of the article or articles introduced or attempted to be introduced.

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19 U.S.C. § 1592. Penalties for fraud, gross negligence, and negligence

(a) Prohibition

(1) General rule

Without regard to whether the United States is or may be deprived of all or a portion of any lawful duty, tax, or fee thereby, no person, by fraud, gross negligence, or negligence –

(A) may enter, introduce, or attempt to enter or introduce any merchandise into the commerce of the United States by means of –

(i) any document or electronically transmitted data or information, written or oral statement, or act which is material and false, or

(ii) any omission which is material, or

(B) may aid or abet any other person to violate subparagraph (A).

* * *

(c) Maximum penalties

(1) Fraud

A fraudulent violation of subsection (a) of this section is punishable by a civil penalty in an amount not to exceed the domestic value of the merchandise.

(2) Gross negligence

A grossly negligent violation of subsection (a) of this section is punishable by a civil penalty in an amount not to exceed –

(A) the lesser of –

(i) the domestic value of the merchandise, or

(ii) four times the lawful duties, taxes, and fees of which the United States is or may be deprived, or

(B) if the violation did not affect the assessment of duties, 40 percent of the dutiable value of the merchandise.

(3) Negligence

A negligent violation of subsection (a) of this section is punishable by a civil penalty in an amount not to exceed –

(A) the lesser of –

(i) the domestic value of the merchandise, or

(ii) two times the lawful duties, taxes, and fees of which the United States is or may be deprived, or

(B) if the violation did not affect the assessment of duties, 20 percent of the dutiable value of the merchandise.

* * *

(d) Deprivation of lawful duties, taxes, or fees

Notwithstanding section 1514 of this title, if the United States has been deprived of lawful duties, taxes, or fees as a result of a violation of subsection (a) of this section, the Customs Service shall require that such lawful duties, taxes, and fees be restored, whether or not a monetary penalty is assessed.

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19 C.F.R. § 113.62 Basic Importation and entry bond conditions.

A bond for basic importation and entry shall contain the conditions listed in this section and may be either a single entry or a continuous bond, except that a bond taken in the case of merchandise subject to an exclusion order of the International Trade Commission under 19 U.S.C. 1337 shall be a single entry bond.

Basic Importation and
Entry Bond Conditions

(a) Agreement to Pay Duties, Taxes, and Charges.

(1) If merchandise is imported and released from Customs custody or withdrawn from a Customs bonded warehouse into the commerce of, or for consumption in,

the United States, or under § 181.53 of this chapter is withdrawn from a duty-deferral program for exportation to Canada or Mexico or for entry into a duty-deferral program in Canada or Mexico, the obligors (principal and surety, jointly and severally) agree to:

(i) Deposit, within the time prescribed by law or regulation, any duties, taxes, and charges imposed, or estimated to be due, at the time of release or withdrawal; and

(ii) Pay, as demanded by Customs, all additional duties, taxes, and charges subsequently found due, legally fixed, and imposed on any entry secured by this bond.

* * *

(b) Agreement to Make or Complete Entry. If all or part of imported merchandise is released before entry under the provisions of the special delivery permit procedures under 19 U.S.C. 1448(b), released before completion of the entry under 19 U.S.C. 1484(a), or withdrawn from warehouse under 19 U.S.C. 1557(a) (see § 10.62b of this chapter), the principal agrees to file within the time and in the manner prescribed by law and regulation, documentation to enable Customs to:

(1) Determine whether the merchandise may be released from Customs custody;

(2) Properly assess duties on the merchandise;

(3) Collect accurate statistics with respect to the merchandise; and

(4) Determine whether applicable requirements of law and regulation are met.

* * *

(d) Agreement to Redeliver Merchandise. If merchandise is released conditionally from Customs custody to the principal before all required evidence is produced, before its quantity and value are determined, or before its right of admission into the United States is determined, the principal agrees to redeliver timely, on demand by Customs, the merchandise released if it:

(1) Fails to comply with the laws or regulations governing admission into the United States;

(2) Must be examined, inspected, or appraised as required by 19 U.S.C. 499; or

(3) Must be marked with the country of origin as required by law or regulation.

* * *

(l) Consequence of default.

(1) If the principal defaults on agreements in this condition other than conditions (a), (g) or (i) the obligors agree to pay liquidated damages equal to the value of the merchandise involved in the default, or three times the value of the merchandise involved in the default if the merchandise is restricted merchandise or alcoholic beverages, or such other amount as may be authorized by law or regulation except that in the case of merchandise subject to an exclusion order of the International Trade Commission under 19 U.S.C. 1337 which has been released before such order becomes final, the obligors agree to pay

liquidated damages in the amount specified in the order for failure to redeliver such merchandise.

* * *

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19 C.F.R. § 141.113 Recall of merchandise released from Customs custody.

(a) Merchandise not legally marked. Certain merchandise is required to be marked or labeled pursuant to the following provisions:

(1) Section 304, Tariff Act of 1930, as amended (19 U.S.C. 1304), pertaining to marking with country of origin;

(2) Textile Fiber Products Identification Act (15 U.S.C. 70);

(3) Wool Products Labeling Act (15 U.S.C. 68);

(4) Fur Products Labeling Act (15 U.S.C. 69); and

(5) Chapter 91, Additional U.S. Note 4, Harmonized Tariff Schedule of the United States (HTSUS), pertaining to special marking for watch and clock movements, cases, and dials.

If such merchandise is found after release to be not legally marked, the port director may demand its return to Customs custody for the purpose of requiring it to be properly marked or labeled. The demand for marking or labeling shall be made not later than 30 days after the date of entry in the case of merchandise examined in

public stores, and places of arrival, such as docks, wharfs, or piers. Demand may be made no later than 30 days after the date of examination in the case of merchandise examined at the importer's premises or such other appropriate places as determined by the port director.

(b) Textiles and textile products. For purposes of determining whether the country of origin of textiles and textile products subject to the provisions of § 12.130 of this chapter has been accurately represented to Customs, the release from Customs custody of any such textile or textile product shall be deemed conditional during the 180-day period following the date of release. If the port director finds during the conditional release period that a textile or textile product is not entitled to admission into the commerce of the United States because the country of origin of the textile or textile product was not accurately represented to Customs, he shall promptly demand its return to Customs custody. Notwithstanding the provisions of paragraph (h) of this section and § 113.62(l)(1) of this chapter, a failure to comply with a demand for return to Customs custody made under this paragraph shall result in the assessment of liquidated damages equal to the value of the merchandise involved.

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19 U.S.C. § 1304. Marking of imported articles and containers

(a) Marking of articles

Except as hereinafter provided, every article of foreign origin (or its container, as provided in subsection (b) hereof) imported into the United States shall be marked in a conspicuous place as legibly, indelibly, and permanently as the nature of the article (or container) will permit in such manner as to indicate to an ultimate purchaser in the United States the English name of the country of origin of the article. . . .

* * *

(h) Additional duties for failure to mark

If at the time of importation any article (or its container, as provided in subsection (b) of this section) is not marked in accordance with the requirements of this section, and if such article is not exported or destroyed or the article (or its container, as provided in subsection (b) of this section) marked after importation in accordance with the requirements of this section (such exportation, destruction, or marking to be accomplished under customs supervision prior to the liquidation of the entry covering the article, and to be allowed whether or not the article has remained in continuous customs custody), there shall be levied, collected, and paid upon such article a duty of 10 per centum ad valorem, which shall be deemed to have accrued at the time of importation, shall not be construed to be penal, and shall not be remitted wholly or in part nor shall payment thereof be avoidable for any cause. Such duty shall be levied, collected, and paid in addition to any other duty imposed by law and

whether or not the article is exempt from the payment of ordinary customs duties. The compensation and expenses of customs officers and employees assigned to supervise the exportation, destruction, or marking to exempt articles from the application of the duty provided for in this subsection shall be reimbursed to the Government by the importer.

(i) Delivery withheld until marked

No imported article held in customs custody for inspection, examination, or appraisement shall be delivered until such article and every other article of the importation (or their containers), whether or not released from customs custody, shall have been marked in accordance with the requirements of this section or until the amount of duty estimated to be payable under subsection (h) of this section has been deposited. Nothing in this section shall be construed as excepting any article (or its container) from the particular requirements of marking provided for in any other provision of law.

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15 U.S.C. § 45. Unfair methods of competition unlawful; prevention by Commission

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(m) Civil actions for recovery of penalties for knowing violations of rules and cease and desist orders respecting

unfair or deceptive acts or practices; jurisdiction; maximum amount of penalties; continuing violations; de novo determinations; compromise or settlement procedure

(1)(A) The Commission may commence a civil action to recover a civil penalty in a district court of the United States against any person, partnership, or corporation which violates any rule under this chapter respecting unfair or deceptive acts or practices (other than an interpretive rule or a rule violation of which the Commission has provided is not an unfair or deceptive act or practice in violation of subsection (a)(1) of this section) with actual knowledge or knowledge fairly implied on the basis of objective circumstances that such act is unfair or deceptive and is prohibited by such rule. In such action, such person, partnership, or corporation shall be liable for a civil penalty of not more than $10,000 for each violation.

(B) If the Commission determines in a proceeding under subsection (b) of this section that any act or practice is unfair or deceptive, and issues a final cease and desist order, other than a consent order, with respect to such act or practice, then the Commission may commence a civil action to obtain a civil penalty in a district court of the United States against any person, partnership, or corporation which engages in such act or practice –

(1) after such cease and desist order becomes final (whether or not such person, partnership, or corporation was subject to such cease and desist order), and

(2) with actual knowledge that such act or practice is unfair or deceptive and is unlawful under subsection (a)(1) of this section.

In such action, such person, partnership, or corporation shall be liable for a civil penalty of not more than $10,000 for each violation.

(C) In the case of a violation through continuing failure to comply with a rule or with subsection (a)(1) of this section, each day of continuance of such failure shall be treated as a separate violation, for purposes of subparagraphs (A) and (B). In determining the amount of such a civil penalty, the court shall take into account the degree of culpability, any history of prior such conduct, ability to pay, effect on ability to continue to do business, and such other matters as justice may require.

(2) If the cease and desist order establishing that the act or practice is unfair or deceptive was not issued against the defendant in a civil penalty action under paragraph (1)(B) the issues of fact in such action against such defendant shall be tried de novo. Upon request of any party to such an action against such defendant, the court shall also review the determination of law made by the Commission in the proceeding under subsection (b) of this section that the act or practice which was the subject of such proceeding constituted an unfair or deceptive act or practice in violation of subsection (a) of this section.

(3) The Commission may compromise or settle any action for a civil penalty if such compromise or settlement is accompanied by a public statement of its reasons and is approved by the court.

* * *

15 U.S.C. § 70a. Violations of Federal Trade Commission Act

(a) Introduction or manufacture for introduction into commerce, sale, advertising or offering for sale in commerce

The introduction, delivery for introduction, manufacture for introduction, sale, advertising, or offering for sale, in commerce, or the transportation or causing to be transported in commerce, or the importation into the United States, of any textile fiber product which is misbranded or falsely or deceptively advertised within the meaning of this subchapter or the rules and regulations promulgated thereunder, is unlawful, and shall be an unfair method of competition and an unfair and deceptive act or practice in commerce under the Federal Trade Commission Act [15 U.S.C. 41 et seq.].

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15 U.S.C. § 70b. Misbranded and falsely advertised textile fiber products

* * *

(b) Stamp, tag, label or other means of identification; contents

Except as otherwise provided in this subchapter, a textile fiber product shall be misbranded if a stamp, tag, label, or other means of identification, or substitute therefor authorized by section 70c of this title, is not on or

affixed to the product showing in words and figures plainly legible, the following:

* * *

(4) If it is an imported textile fiber product the name of the country where processed or manufactured.

* * *

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15 U.S.C. § 70e. Enforcement

(a) Enforcement by Federal Trade Commission

Except as otherwise specifically provided herein, this subchapter shall be enforced by the Federal Trade Commission under rules, regulations, and procedure provided for in the Federal Trade Commission Act [15 U.S.C. 41 et seq.].

(b) Terms of Federal Trade Commission Act incorporated into this subchapter

The Commission is authorized and directed to prevent any person from violating the provisions of this subchapter in the same manner, by the same means, and with the same jurisdiction, powers, and duties as though all applicable terms and provisions of the Federal Trade Commission Act [15 U.S.C. 41 et seq.] were incorporated into and made a part of this subchapter; and any such person violating the provisions of this subchapter shall be subject to the penalties and entitled to the privileges and immunities provided in said Federal Trade Commission

Act, in the same manner, by the same means, and with the same jurisdiction, powers, and duties as though the applicable terms and provisions of the said Federal Trade Commission Act were incorporated into and made a part of this subchapter.

(c) Rules and regulations by Federal Trade Commission

The Commission is authorized and directed to make such rules and regulations, including the establishment of generic names of manufactured fibers, under and in pursuance of the terms of this subchapter as may be necessary and proper for administration and enforcement.

(d) Inspection, analyses, tests, etc.

The Commission is authorized to cause inspections, analyses, tests, and examinations to be made of any product subject to this subchapter.

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UNITED STATES DISTRICT COURT

CENTRAL DISTRICT OF CALIFORNIA

WESTERN DIVISION

UNITED STATES OF AMERICA ex rel. AMERICAN TEXTILE MANUFACTURERS INSTITUTE, INC.,	**CASE NO CV96-6765 HLH (RCx)**
Plaintiffs,	**AMENDED COMPLAINT FOR VIOLATION OF FALSE CLAIMS ACT**
v.	
THE LIMITED, INC.; THE LIMITED LONDON-PARIS-NEW YORK, INC.; LIMITED TOO, INC.; INTIMATE BRANDS, INC.; VICTORIA'S SECRET STORES, INC.; VICTORIA'S SECRET CATALOGUE, INC.; CACIQUE, INC.; EXPRESS, INC.; LERNER	**[FILED UNDER SEAL PURSUANT TO 31 U.S.C. § 3730(b)]**
	(Filed Mar. 21, 1997)

NEW YORK, INC.; LANE BRYANT, INC.; HENRI BENDEL, INC.; STRUCTURE, INC.; ABERCROMBIE & FITCH, INC.; MAST INDUSTRIES, INC.; TARRANT APPAREL GROUP, d/b/a FASHION RESOURCE, INC.; GERARD GUEZ; and TODD KAY,	)
Defendants.	)

Relator, American Textile Manufacturers Institute, Inc., (hereinafter "ATMI") by its attorneys, for its Amended Complaint alleges:

JURISDICTION AND VENUE

1. This action arises under 31 U.S.C. § 3729 *et seq.*, also known as the "False Claims Act." This Court has jurisdiction over this action pursuant to 31 U.S.C. § 3732(a).

2. This Court has personal jurisdiction over all Defendants pursuant to section 410.10 of the California Code of Civil Procedure in that Defendants have transacted and are continuing to transact substantial business within the State of California and this District by (a) importing or causing to be imported textile and apparel products into the United States through the Los Angeles, Long Beach Seaport Area (formerly known as the Los Angeles Customs District), and/or (b) operating numerous retail stores for the sale of such apparel products in the State and this District. The claims asserted

herein arise out of the transaction of such business in the State of California and this District.

3. Venue is proper in this District pursuant to 28 U.S.C. § 1391(b)(2) in that one or more of the acts or omissions proscribed by 31 U.S.C. § 3729 took place within this judicial District.

NATURE OF THE ACTION

4. The importation of apparel products is subject to certain quantitative restrictions or quotas negotiated by the United States and established on a country-by-country basis in various multilateral and bilateral agreements. Imported apparel products subject to such restrictions must be accompanied by appropriate export documents to demonstrate that such merchandise falls within established quantitative limitations. Once a particular country exhausts its quota for a given product category during a given period of time, no further importations are allowed and goods presented for entry into the United States for consumption must be denied entry by the U.S. Customs Service (hereinafter "Customs").

5. On or about September 25, 1995, ATMI initiated an investigation into the circumstances surrounding the importation of apparel products by and/or on behalf of Defendants to determine whether Defendants were knowingly making, using, or causing to be made or used false records or statements to Customs "to conceal, avoid, or decrease an obligation to pay or transmit money or property to the Government" within the meaning of the False Claims Act, 31 U.S.C. § 3729(a)(7). ATMI's investigation has revealed, and ATMI hereby alleges, that

Defendants, together and each of them individually, have engaged in a pattern or practice of trade pursuant to which articles of apparel produced in the People's Republic of China have been transshipped to Hong Kong or Macau; have been falsely labelled as the products of Hong Kong or Macau; and have been knowingly represented to be the products of Hong Kong or Macau in official entry documents submitted to Customs by or on behalf of said Defendants.

6. The false records or statements made by Defendants have permitted them to evade country-specific quota restrictions and to conceal from Customs and thereby avoid their obligations to (a) forfeit the merchandise or its value to the United States pursuant to 18 U.S.C. § 545; (b) pay civil penalties equal to the value of the merchandise pursuant to 19 U.S.C. § 1595a(b); (c) pay civil penalties not to exceed the domestic value of the merchandise pursuant to 19 U.S.C. § 1592; (d) pay liquidated damages equal to the value of the merchandise pursuant to 19 C.F.R. §§ 113.62(k)(1) and 141.113 for breach of their Customs bonds; (e) pay a ten percent (10%) *ad valorem* marking duty upon the importation of articles marked with an erroneous country of origin pursuant to 19 U.S.C. § 1304(f); and (f) pay a civil penalty for unfair methods of competition or unfair and deceptive acts or practices within the meaning of and pursuant to the Textile Fiber Products Identification Act and the Federal Trade Commission Act, 15 U.S.C. §§ 45(m) and 70a.

PARTIES

7. Relator ATMI is the national trade association of the domestic textile industry. For many years, ATMI has represented the interests of its members by addressing various forms of unfair and excessive import competition under federal statutes and international agreements governing international trade. ATMI has pursued numerous initiatives with the U.S. Congress and various departments and agencies of the Executive Branch in an effort to combat the transshipment and mislabeling of the country of origin of textile and apparel products. Such transshipment and mislabeling are undertaken for the purpose of evading the lawful quota restrictions placed upon the importation of textile and apparel products.

8. Defendant The Limited, Inc. is a corporation organized under the laws of the State of Delaware with its principal place of business at Three Limited Parkway, Columbus, Ohio 43216. The Limited, Inc. and certain of its wholly-owned subsidiaries own and operate retail establishments throughout the United States, including within the State of California and this judicial District, that are engaged in the sale of women's and/or men's apparel and miscellaneous fashion accessories.

9. Defendant The Limited London-Paris-New York, Inc. is a corporation organized under the laws of the State of Delaware with its principal place of business at Three Limited Parkway, Columbus, Ohio 43216. The Limited London-Paris-New York, Inc. is a wholly-owned subsidiary of LIM Holding Corporation, a Delaware corporation

which in turn is a wholly-owned subsidiary of The Limited, Inc. The Limited London-Paris-New York, Inc. is a retailer of women's clothing.

10. Defendant Limited Too, Inc. is a corporation organized under the laws of the State of Delaware with its principal place of business at P.O. Box 182145, Columbus, Ohio 43218. The Limited Too, Inc. is a wholly-owned subsidiary of Limited Too Holding Corporation, a Delaware corporation and a wholly-owned subsidiary of The Limited, Inc. Limited Too, Inc. is a retailer of casual girls' apparel.

11. Prior to October 24, 1995, Defendant The Limited, Inc. offered women's intimate apparel to the retail market in the United States through three wholly-owned subsidiaries or divisions known as Victoria's Secret, Inc., Victoria's Secret Catalogue, Inc., and Cacique, Inc. On or about October 24, 1995, Defendant The Limited, Inc. spun off these divisions or subsidiaries, together with other business entities not here relevant, into a separate corporation known as Intimate Brands, Inc.

12. Defendant Intimate Brands, Inc. (hereinafter "IBI") is a corporation organized under the laws of the State of Delaware with its principal place of business at Three Limited Parkway, Columbus, Ohio 43230. IBI is a majority-owned subsidiary of The Limited, Inc. As of February 3, 1996, The Limited, Inc. owned eighty-three percent (83%) of the shares of IBI, which are traded on the New York Stock Exchange. IBI retails women's intimate apparel and personal care products through its three divisions known as Victoria's Secret Stores, Inc., Victoria's Secret Catalogue, Inc. and Cacique, Inc.

13. Defendant Victoria's Secret Stores, Inc. is a corporation organized under the laws of the State of Delaware with its principal place of business at Four Limited Parkway East, Reynoldsburg, Ohio 43068. Victora's [sic] Secret Stores, Inc. is a wholly-owned subsidiary of Victoria's Secret Holding Corporation, a Delaware corporation that is a wholly-owned subsidiary of IBI.

14. Defendant Victoria's Secret Catalogue, Inc. is a corporation organized under the laws of the State of Delaware with its principal place of business at 3425 Stelzer Road, Columbus, Ohio 43218. Victora's [sic] Secret Stores, Inc. is a wholly-owned subsidiary of Victoria's Secret Catalogue Holding Corporation, a Delaware corporation that is a wholly-owned subsidiary of IBI.

15. Defendant Cacique, Inc. is a corporation organized under the laws of the State of Delaware with its principal place of business at Five Limited Parkway East, Columbus, Ohio 43218. Cacique, Inc. is a wholly-owned subsidiary of Cacique Holding Corporation, a Delaware corporation that is a wholly-owned subsidiary of IBI.

16. Defendant Express, Inc. is a corporation organized under the laws of the State of Delaware with its principal place of business at One Limited Parkway, Columbus, Ohio 43230. Express, Inc. is a wholly-owned subsidiary of Express Holding Corporation, a Delaware corporation and a wholly-owned subsidiary of The Limited, Inc. Express, Inc., d/b/a Compagnie Internationale Express, sells popular-priced women's sportswear and accessories.

17. Defendant Lerner New York, Inc. is a corporation organized under the laws of the State of Delaware

with its principal place of business at 460 West 33rd Street, 5th Floor, New York, New York 10001. Lerner New York, Inc. is a wholly-owned subsidiary of Lerner Holding Corporation, a Delaware corporation and a wholly-owned subsidiary of The Limited, Inc. Lerner New York, Inc. is a retailer of popular and budget-priced women's specialty apparel.

18. Defendant Lane Bryant, Inc. is a corporation organized under the laws of the State of Delaware with its principal place of business at Five Limited Parkway, Reynoldsburg, Ohio 43068. Lane Bryant, Inc. is a wholly-owned subsidiary of Lane Bryant Holding Corporation, a Delaware corporation and a wholly-owned subsidiary of The Limited, Inc. Lane Bryant, Inc. operates specialty stores with a focus on women's special-size sportswear, ready-to-wear coats and intimate apparel.

19. Defendant Henri Bendel, Inc. is a corporation organized under the laws of the State of Delaware with its principal place of business at 20 West 43rd Street, 9th Floor, New York, New York 10036. Henri Bendel is a wholly-owned subsidiary of Henri Bendel Holding Corporation, a Delaware corporation and a wholly-owned subsidiary of The Limited, Inc. It is a retailer of fashion apparel, cosmetics, accessories and gifts for women.

20. Defendant Structure, Inc. is a corporation organized under the laws of the State of Delaware with its principal place of business at Two Limited Parkway, Columbus, Ohio 43218. Structure, Inc. is a wholly-owned subsidiary of Structure Holding Corporation, a Delaware

corporation and a wholly-owned subsidiary of The Limited, Inc. It is a retailer of men's sportswear and ready-to-wear apparel.

21. Defendant Abercrombie & Fitch, Inc. is a corporation organized under the laws of the State of Delaware with its principal place of business at Four Limited Parkway East, Columbus, Ohio 43218. Abercrombie & Fitch, Inc. is a majority-owned subsidiary of The Limited, Inc. Following a proposed public offering of shares in Defendant Abercrombie & Fitch, Inc., The Limited, Inc. is expected to retain between 84.2 and 86.0 percent of the economic interest in said Defendant and between 94.1 and 94.9 percent of the combined voting power of the shares of said Defendant. Abercrombie & Fitch, Inc. is a retailer of men's and women's sportswear.

22. Defendant Mast Industries, Inc. (hereinafter "Mast (US)") is a corporation organized under the laws of the State of Delaware with its principal place of business at 100 Old River Road, P.O. Box 2020, Andover, Massachusetts 01810. Mast Industries, Inc. is a wholly-owned subsidiary of Mast Holding Corporation, a Delaware corporation and a wholly-owned subsidiary of The Limited, Inc. Mast (US) is a contract manufacturer of apparel for men, women, and children. Mast (US) is engaged in the importation and distribution of apparel products solely to retail stores and catalogue sales companies owned by or affiliated with The Limited, Inc. in the United States, including IBI and its subsidiaries and Abercrombie & Fitch, Inc.

23. Defendant Mast (US) owns and controls a subsidiary known as Mast Industries (Far East) Ltd. (hereinafter "Mast (FE)"). Mast (FE) maintains its principal place of business at 14/F East Wing, New World Office Building, 24 Salisbury Road, Kowloon, Hong Kong. Mast (FE) procures apparel on a contract basis from manufacturers throughout the Far East, including Hong Kong, Macau, and the People's Republic of China. Mast (FE) only contracts for the production or importation of apparel products for sale to entities within the United States that are owned or controlled by The Limited, Inc.

24. Except where otherwise noted, further references in this Complaint to "the Limited Defendants" should be read as including The Limited, Inc. and each of its domestic subsidiaries or divisions referenced in paragraphs 8 through 22 hereof.

25. Defendant Tarrant Apparel Group (hereinafter "Tarrant (US)") is a corporation organized and existing under the laws of the State of California with its principal place of business at 3151 East Washington Boulevard, Los Angeles, California 90023. Tarrant (US) is a contract manufacturer of apparel. Upon information and belief, Tarrant (US) was incorporated in September 1988 under the name Fashion Resource, Inc. Tarrant (US) continues to use the name Fashion Resource, Inc. in the United States as a trade name. Most of the import transactions undertaken by Tarrant (US) that are at issue in this Complaint have been documented with Customs under the name of Fashion Resource, Inc.

26. Defendant Tarrant (US) owns and controls a subsidiary known as Tarrant Company Limited (hereinafter "Tarrant (HK)"). Tarrant (HK) is organized under the laws of Hong Kong and maintains a place of business at 13/F Liadro Center, 72-80 Hoi Yuen Road, Kwun Tong, Kowloon, Hong Kong. Tarrant (HK) procures apparel on a contract basis from manufacturers throughout the Far East, including Hong Kong, Macau, and the People's Republic of China. Tarrant (HK) exports or causes to be exported apparel products exclusively to Tarrant (US). Tarrant (US), d/b/a Fashion Resource, Inc., is the importer of record for substantially all of the textile and apparel products exported to the United States by Tarrant (HK). Tarrant (US) resells apparel products acquired from Tarrant (HK) to various retail establishments in the United States, including the Limited Defendants.

27. Defendant Gerard Guez is a citizen of the State of California and was one of the original shareholders of Fashion Resource, Inc. and remains one of the principal shareholders of Tarrant (US). At all times material to this Complaint, Gerard Guez has served as Chairman and Chief Executive Officer of Tarrant (US). Mr. Guez is personally involved in the day-to-day operations of Defendant Tarrant (US), including transactions that are the subject matter of this Complaint. Mr. Guez is named as a Defendant herein in his individual capacity.

28. Defendant Todd Kay is a citizen of the State of California and was one of the original shareholders of Fashion Resource, Inc. and remains one of the principal shareholders of Tarrant (US). At all times material to this Complaint, Todd Kay has served as President of Tarrant (US). Mr. Kay has been personally involved in the day-to-

day operations of Defendant Tarrant (US), including transactions that are the subject matter of this Complaint. Mr. Kay is named as a Defendant herein in his individual capacity.

DESCRIPTION OF THE TEXTILE AND APPAREL IMPORT CONTROL PROGRAM

29. The United States is a party to the Uruguay Round Final Act Agreement on Textiles and Clothing ("ATC"), the successor to the Arrangement Regarding International Trade in Textiles, also known as the "Multifiber Arrangement" or "MFA." Both the MFA, which was in force from January 1, 1974 to December 31, 1995, and its successor, the ATC, provide a general framework and a series of guidelines for the imposition of quantitative restraints (or quotas) on signatories' exports of textile products to the United States. The United States' accession to the MFA was authorized by section 204 of the Agricultural Act of 1956, 7 U.S.C. § 1854, which also authorizes the President to enter into bilateral agreements with other countries to limit exports of "any agricultural commodity or product manufactured therefrom or textiles or textile products." Section 204 also authorizes the President to issue regulations governing the entry into domestic commerce or withdrawal from warehouse of any such products, including textiles or textile products, and to carry out the bilateral agreements concluded under the section. Section 332 of the Uruguay Round Agreements Act, Pub. L. No. 103-465, 108 Stat. 4809 (1994), amended section 204 of the Agricultural Act of 1956 to authorize the United States' participation in the ATC. *See* 7 U.S.C. § 1854.

30. Under the auspices of the MFA and the ATC, the United States has entered into bilateral agreements with forty-five (45) countries limiting those countries' exports of textiles and textile products to the United States. Additionally, the United States has entered into bilateral agreements with eleven (11) countries that are not parties to the ATC, limiting their exports of textiles and clothing to the United States. These agreements are authorized by section 204 of the Agricultural Act, 7 U.S.C. § 1854. Included among these agreements are bilateral agreements with Hong Kong (ATC), Macau (ATC) and the People's Republic of China (section 204). The agreements establish quota levels for groups of products such as yarns, fabrics, apparel, and made-up textile products. Further, within each group of products, specific quotas are set for individual items.

31. By Executive Order 11,651, the President established the Committee for the Implementation of Textile Agreements ("CITA"), consisting of representatives from the Departments of State, Treasury, Labor, Commerce and the Office of the United States Trade Representative. Exec. Order No. 11,651, 37 Fed. Reg. 4699 (1972). The Commerce representative serves as Chairman of CITA. While CITA sets policy and generally administers the various agreements, including the establishment of quota levels, actual enforcement of the textile import program lies with the Secretary of Treasury, and specifically with Customs. Customs has issued detailed procedural and documentary requirements regarding the importation of textiles and apparel products under the various agreements. Customs also administers the quotas established by these agreements.

32. Central to the administration of the textile import program are detailed rules for determining country of origin for purposes of attributing a particular import to the applicable country-specific quota. The internationalization of production that characterizes the textile and apparel industry has necessitated the establishment of such rules, because manufacturers will often move fabric and materials from country to country through the various stages of the production process.

33. Under applicable Customs' regulations, a textile or textile product is the product of a particular foreign country if it is "wholly the growth, product or manufacture" of that foreign country. 19 C.F.R. § 12.130(b). If, however, the product consists of materials produced or derived from, or processed in more than one foreign country, it shall, prior to July 1, 1996, be considered the product of the foreign country where it last underwent a substantial transformation. *See id.* A product will be considered to have undergone a substantial transformation if it has been transformed by means of a substantial manufacturing or processing operation into a new and different article of commerce. *Id.*

34. Under rulings previously issued by Customs, the countries of origin of some textile products, particularly apparel, were often determined by where the fabric components of the finished article were cut to shape. The bulk of the products that are the subject of this Complaint were generally subject to this fabric cutting rule. The recent enactment of the Uruguay Round Agreements Act, however, has resulted in a change in the rule of origin. Section 334(b) of the Act, effective on July 1, 1996, provides that the country of origin of a textile or apparel

product shall be determined on the basis of where the most important assembling or manufacturing process occurs. 19 U.S.C. § 3592(b)(3)(A). Customs has issued detailed rules of origin implementing the change in policy brought about by the Uruguay Round Agreements Act. *See* 19 C.F.R. § 102.21.

35. Customs' regulations require that all importations of textiles or textile products subject to section 204 of the Agricultural Act be accompanied by declarations prepared by the manufacturer(s), producer(s), exporter(s) or importer of such products. 19 C.F.R. § 12.130(f). Where the textiles or textile products are each wholly the growth, product, or manufacture of a single foreign territory or country or insular possession of the United States, or were assembled in the single foreign territory or country or insular possession of the United States, or are fabricated components which are in whole the product of the United States and/or a single foreign territory or country or insular possession of the United States, the declaration must identify the country of origin of each imported article. *Id.* § 12.130(f)(1). Where the textiles or textile products were subjected to manufacturing or processing operations in, and/or incorporate materials originating in, more than one foreign territory or country or U.S. insular possession, or were assembled in, and/or incorporate fabricated components which are the product of the United States and more than one foreign territory or country or U.S. insular possession, the declaration must provide, with respect to each imported article, detailed information on (1) the various manufacturing and/or processing operations, including the nature of each operation, the date on which it was performed, the

country in which it was performed, and the date on which the article was exported from each such country, and (2) a description of each material, the country in which it was produced, and the date it was exported. *Id.* § 12.130(f)(2). All such declarations include a certification that the information set forth therein is correct and true to the best of the declarants' information, knowledge, and belief.

EVIDENCE OF FALSE RECORDS OR STATEMENTS BY THE LIMITED DEFENDANTS

36. The Limited Defendants import directly approximately fifty-five percent (55%) of the apparel sold by them at retail. The principal source of these imports is from the Far East, including Hong Kong, Macau, and the People's Republic of China. In addition, merchandise acquired by the Limited Defendants from domestic sources, including Tarrant (US), d/b/a Fashion Resource, Inc. is also imported. The Limited Defendants acquire merchandise from a diversified group of suppliers, with no one supplier providing more than five percent (5%) of said Defendants' annual purchases.

37. The domestic market for men's and women's apparel is intensely competitive. In its 1994 Form 10-K Report to the U.S. Securities and Exchange Commission, The Limited, Inc. stated that it competes on the basis of the design, price, and quality of its merchandise.

38. Through their integrated operations, the Limited Defendants hold themselves out as being able to control all aspects of the design, development, sourcing, and distribution of their products. The control exercised

by the Limited Defendants over the production of garments for them by factories in the Far East including the People's Republic of China is well documented in two cases currently pending in the U.S. Tax Court. *The Limited, Inc. and Consolidated Subsidiaries v. Commissioner of Internal Revenue*, U.S. Tax Court Docket No. 12004-94 and 26618-95. In both Tax Court cases, the Limited Defendants, as petitioners, claimed that Mast FE should have been treated as a manufacturer under I.R.C. § 954. The Limited Defendants described the sourcing activities that Mast FE performed on behalf of The Limited, Inc. in paragraph 4(b) of its petition in Docket NO. 12004-94 as follows:

> selecting and qualifying factories; having sample garments made; suggesting modifications for the samples to the buyers; negotiating the cost to manufacture the garments with factories; supplying test orders of garments; . . . performing quality control during and after manufacturing; preparing market reports; providing quota for export of garments; resolving fabric and manufacturing problems; and arranging for shipment and delivery within about forty-five to sixty days of the placement of the order.

The Limited, Inc. alleged that Mast FE micro-managed every thing from preproduction to quality control, regardless of the number of contractors involved. Mast FE

> typically conducted preproduction meetings with factory personnel prior to beginning production. If multiple factories were used for an order, the multiple factories' personnel often

> attended the meetings. . . . At some of the pre-production meetings, techniques used by one factory were passed by MFE to other factories to ensure high quality and consistency among the garments in the order.

Petition at ¶ 5(b)(2); Petitioner's Supplemental Memorandum of Points and Authorities in Opposition to Respondent's Motion for Partial Summary Judgement at 13. Sworn declarations made by senior executives of the Limited Defendants support the factual allegations in the petitions. John R. Welch, then-President of Mast FE, stated "[a]lthough MFE did not have any financial interest in contractors such as sewing factories, they were acting under MFE's direction." According to Welch, Mast FE

> planned, scheduled, and monitored numerous dates for the final production of garments, including dates for final color details, for delivery of the fabric to contractors, for quality control inspections, for color testing, and for final delivery dates for finished garments. Its quality inspectors worked at contractors' facilities, often on a daily basis, checking fabric before cutting, conducting in-line inspection of garments while the garments were being sewn, making suggestions to improve the production process, and conducting final approvals of completed orders.

Curtis Fletcher, the Director of Product Coordination of Express, stated in his declaration that he traveled to the Far East as many as six times a year to visit the facilities of the actual garment manufacturers. Declarations of John R. Welch and Curtis Fletcher attached to Petitioner's

Notice of Objection to Respondent's Motion for Partial Summary Judgment.

39. The Limited Defendants purchase millions of yards of fabric each year from independent suppliers. The Limited Defendants supply this fabric to the manufacturers that produce garments, the designs and specifications for which are established by said Defendants.

40. The Limited Defendants maintain strict quality control standards and work directly with their suppliers at the plant level to insure that quality standards are met.

41. The Limited Defendants compete with apparel retailers and others for the availability of production facilities and quota capacity in the Far East, including Hong Kong, Macau, and the People's Republic of China.

42. As a result of the competition with other retailers for reliable sources of production and available quota, coupled with the need to monitor the quality of the products produced by their suppliers and to safeguard the millions of yards of fabric entrusted to garment manufacturers each year, the Limited Defendants are in a position to and do monitor the origin-conferring activities of the manufacturers that produce textile and apparel products for them. As a consequence, representations made by or on behalf of the Limited Defendants to Customs with respect to the country of origin of imported textile and apparel products marketed by said Defendants are based upon actual knowledge of the origin-conferring activities of their suppliers, or are made in deliberate ignorance of these activities or with reckless disregard for the truth or falsity of their representations with respect to such activities.

False Claims With Respect To Products Supplied By Gaddy Garment Factory Ltd.

43. Gaddy Garment Factory Ltd. (hereinafter "Gaddy (HK)") is a major supplier of garments to the Limited Defendants purchasing through Mast (FE). Gaddy (HK) is located at 11/F, Unit C, East Sun Industrial Building, 16 Shing Yip Street, Kwun Tong, Kowloon, Hong Kong.

44. At all times material to this Complaint, Gaddy (HK) was in receipt of and/or was in the process of fulfilling purchase orders for apparel submitted to it by Mast (FE) on behalf of the Limited Defendants. Documents obtained from Gaddy (HK) disclose that between January and October 1995, Gaddy (HK) was under contract to produce over 30,000 garments per month for the Limited Defendants.

45. Between January and June 1996, ATMI's investigators visited Gaddy (HK)'s facilities on at least fourteen (14) occasions. Gaddy (HK)'s facility was closely guarded and protected by personnel and video surveillance equipment. Nevertheless, ATMI's investigators were able to make observations of about one-half of the square footage occupied by Gaddy (HK). A small production area approximately twenty by fifty (20 x 50) feet is believed to exist at this location but was not actually observed. At no time during these visits to Gaddy (HK)'s premises was any production of apparel products observed. At no time did ATMI's investigators observe any indication that Gaddy (HK) was engaged in the cutting of fabric for garment production despite documentation showing that Gaddy ordered more than 180,000 yards of fabric to be

delivered to its offices in Hong Kong in January 1996 alone. At no time did ATMI's investigators observe pieces of cut fabric being taken from Gaddy's (HK) premises for processing elsewhere. At no time did ATMI's investigators observe evidence of Gaddy (HK) discarding fabric scraps, remnants of thread or other residue or debris that normally would be generated by a garment factory that was cutting fabric or otherwise producing the quantities of apparel that Gaddy (HK) was under contract to produce.

46. ATMI estimates that in order to wholly produce 30,000 garments per month of the type shipped to the Limited Defendants, Gaddy (HK) would have to employ at least eighty (80) workers full time. A workforce of this size was not deployed nor could it have been deployed at Gaddy's small facility in the East Sun Industrial Building.

47. On the basis of this evidence, ATMI hereby alleges that between January and June 1996, Gaddy (HK) was not engaged at a commercially significant level in the cutting of fabric to shape, the sewing of fabric pieces, or any other operation regarded by Customs as conferring origin on apparel products.

48. Other than general office and clerical activities, the only other activities observed by ATMI's investigators at Gaddy (HK) indicates that this facility operated as a transshipment point. On several occasions, plastic polybags with "Made in China" markings stuffed into other polybags marked "Made In Hong Kong" were observed at Gaddy (HK).

49. On the basis of observations made by ATMI's investigators at Gaddy (HK), it is evident that a person

monitoring Gaddy (HK)'s operations would know or ought to know that Gaddy (HK) was not producing apparel of Hong Kong origin at its facilities in the East Sun Industrial Building.

50. Documentary evidence obtained by ATMI at Gaddy (HK) establishes that, at all times relevant to this Complaint, Gaddy (HK) filled its orders for the Limited Defendants primarily from two sources in the People's Republic of China: Gaddy Garment (China) Factory in Xixiang, Bao An County, Shenzhu, Guangdong, China (hereinafter "Gaddy (PRC)" or "Xixiang") and the Panyu Embroidery Garment Factory (hereinafter "Panyu") located at No. 1 Nanti Xi Road, Shiqiao Panyu, Guangdong, China.

51. Based upon observations made by ATMI's investigators in Guangdong Province, China, it is known that each of these facilities in China, individually and in collaboration, is engaged in the full range of production activities needed to cut fabric and make apparel products, including all activities necessary for conferring country of origin status under applicable U.S. law. Documents obtained by ATMI further disclose that Gaddy (PRC) routinely sent faxes to Gaddy (HK) requesting supplies such as fabric, buttons, accessories, sewing needles, cutting blades, paper for cutting tables, labels and thread. Nearly every one of these requests by Gaddy (PRC) was associated with the production of specific purchase orders by Mast (HK). In addition, Gaddy (HK) sent regular faxes to Gaddy (PRC) and Panyu establishing fabric cutting schedules and production changes, and addressing quality control problems and shipment deadlines, among other things. Faxes confirming production and

delivery schedules for Mast (HK)'s orders were routinely exchanged between Gaddy (HK) and its subcontractors or affiliates in China. Finally, Gaddy (HK) issued specific directions for the printing of cartons with "Made in Hong Kong" marks for the shipment of garments fully cut, made and finished in China. These directions for preparing cartons were linked to numerous orders for Mast (HK).

52. Further documentary evidence obtained by ATMI establishes that Gaddy (HK) routinely notified inspectors at Mast (HK) when certain production orders were complete and ready for inspection. With respect to at least thirty (30) production orders, Gaddy (HK) issued production status sheets to Mast (HK) dated October 20, October 30, November 4 and November 11, 1995, that identified the location of production as either Gaddy (PRC) or Panyu. In particular, the October 20, 1995 production status sheet advised Mast (HK) as to which factory in China, Gaddy (PRC) or Panyu, had the finished garments ready for inspection. In one instance, Gaddy (PRC) instructed Mast (HK) to inspect production order number PA5251 at Gaddy (PRC). This order was to be shipped to Victoria's Secret Catalogue in Columbus, Ohio under Mast Purchase Order No. 06400540 (Style No. VSC3187).

53. ATMI also obtained documentation concerning a Mast (FE) purchase order for peach and blue boxers (Style No. VSC1263) that Gaddy was to have supplied and shipped to Columbus, Ohio, on July 15, 1995. Correspondence from Panyu in China discloses that the fabric was cut and the garments were in fact made in China,

and were to be delivered to Gaddy in Hong Kong on July 15th.

54. The vast majority of garments produced for Gaddy (HK) by Gaddy (PRC) and Panyu are marked "Made in Hong Kong." Gaddy (HK)'s production records disclosed no discernable [sic] basis for marking one garment "Made in Hong Kong" and another garment "Made in China."

False Claims With Respect To The Products Supplied By Shun Tat Fashion Manufactory Ltd.

55. Shun Tat Fashion Manufactory Ltd. (hereinafter "Shun Tat") is a major supplier of apparel to the Limited Defendants. Shun Tat is located in the Tung Kin Industrial Building at 192-202 Tsat Tse Mui Road, North Point, Hong Kong. Shun Tat conducts its business from Flats G and H on the fifth floor and Flat F on the eighth floor at this address.

56. At all times material to this Complaint, Shun Tat was in receipt of and/or was in the process of fulfilling purchase orders for apparel submitted to it by Mast (FE) on behalf of the Limited Defendants. Documents obtained from Shun Tat disclose that at all times material to this Complaint, Shun Tat was under contract to supply hundreds of thousands of pieces of apparel products to the Limited Defendants, as well as other apparel importers in the United States.

57. Between January 16 and July 30, 1996, ATMI's investigators visited Shun Tat's Hong Kong facilities on no less than thirty-five (35) occasions. At no time during

any of these visits to Shun Tat's premises was the production of apparel products observed on a scale comparable to Shun Tat's sales volume. Rather, the limited production activities observed at Shun Tat were more consistent with mere label-stitching or sample-marking. At no time did ATMI's investigators observe fabric being cut to shape for production at Shun Tat or pieces of cut fabric being taken from Shun Tat's premises for processing elsewhere. At no time did Shun Tat discard fabric scraps, remnants of thread or other residue or debris that would normally be generated by a garment factory that was cutting fabric to shape or otherwise producing the quantities of apparel that Shun Tat was under contract to produce or supply.

58. On the basis of this evidence, ATMI hereby alleges that between January 16 and July 30, 1996, Shun Tat was not engaged at a commercially significant level in the cutting of fabric to shape, the sewing of fabric pieces, or any other operations regarded by Customs as conferring origin on apparel products.

59. On several occasions between January 16 and July 30, 1996, ATMI's investigators observed finished garments being delivered to Shun Tat by vehicles engaged in cross-border traffic, *i.e.*, with license plates issued by both the People's Republic of China and Hong Kong. On numerous occasions, ATMI's investigators observed workers at Shun Tat repacking garments and placing them in cartons for export to the Limited Defendants. On several occasions, ATMI's investigators observed at Shun Tat's premises discarded plastic polybags bearing the markings "Made In China." On a number of occasions,

ATMI's investigators observed workers at Shun Tat loading bolts of uncut fabric and accessories onto trucks engaged in cross-border traffic.

60. On the basis of observations made by ATMI's investigators at Shun Tat, it is evident that a person monitoring Shun Tat's operations would know or ought to know that Shun Tat was not producing apparel of Hong Kong origin at its facilities in the Tung Kin Industrial Building.

61. Documents obtained by ATMI from Shun Tat confirm that Shun Tat routinely subcontracted for the production of apparel products for the Limited Defendants with factories in the People's Republic of China, and that such apparel products were marked "Made in Hong Kong" prior to importation into the United States.

62. Shun Tat is affiliated with garment factories in Zhaoqing, Guangdong Province, China that have ample capacity to produce apparel in the volumes needed to fill Mast (FE)'s orders. Together, Shun Tat's Hong Kong and China facilities employ 2,100 workers and boast 1,000 sewing machines, 850 of which are located in China. Shun Tat's Hong Kong facilities were only observed to employ thirty to thirty-five (30-35) workers. Shun Tat's combined monthly production capacity, reliant primarily upon its Chinese facilities, is approximately 200,000 garments per month.

63. During February 1996, Mast (FE) submitted to Shun Tat three (3) purchase orders (VSS17046325; VSS17046237; VSS17046236) for a two-piece short set for Victoria's Secret Country Catalogue in Style Numbers VW3562C and VW3562, all to be shipped to the United

States in March and marked "Made in Hong Kong." Shun Tat contracted for the production of the first two orders of these garments with the Chao Zhou Cheong Shun Garment Co., Ltd. (hereinafter "Chao Zhou") , a Chinese garment factory located at the Shun Tat Enterprise Building, 1 Jan Zheng 2 Road, Zhaoqing, Guangdong Province. The third order was subcontracted to Hing Tat Garment Factory (hereinafter "Hing Tat"), also located at the Shun Tat Industrial Building in China.

64. Mast (FE) also submitted to Shun Tat three (3) separate purchase orders (LTD04040632; LTD04040732; LTD04040733) for Style No. 422-SAT for delivery to The Limited, Inc. in March 1996. During this period, correspondence by Shun Tat with Hing Tat in China discloses that the garments were in fact made in China, notwithstanding Mast (FE)'s nominal direction that the goods should be marked "Made in Hong Kong."

65. Mast (FE) submitted a purchase order to Shun Tat for ladies sleepwear (Style No. LBS4451). Shun Tat subcontracted with Parawin Industries Limited (hereinafter "Parawin") in Hong Kong for the production of Style No. LBS4451. Parawin also subcontracted exclusively with Chinese manufacturers to fulfill its production orders. Mast (FE) exported the ladies sleepwear, Style No. LBS4451, to the United States in June 1996. Said sleepwear was falsely marked as the product of Macau.

66. Parawin is located at 2/F and 7/F, Hoi Luen Industrial Center, 55 Hoi Yuen Road, Kowloon, Hong Kong. At no time during ATMI's investigation of Parawin during June through August 1996 was there any evidence

observed that Parawin was engaged in, or had the capacity to engage in, the production of apparel at its facilities in Hong Kong. In fact, documentation confirms, and ATMI hereby alleges, that Parawin subcontracted exclusively with three Chinese manufacturers: Golden Wall Garment Factory Ltd., Silver Wall Garment Manufacturing Co. Ltd., and Kong Wah.

67. ATMI obtained additional documents evidencing that numerous other production orders submitted by Mast (FE) to Shun Tat were forwarded for production to Hing Tat or St. Sarah Garment Manufactory [sic] Co., Ltd., both located in the Shun Tat Enterprise Building, Zhaoqing, Guangdong Province.

Conclusion With Respect To The Limited Defendants

68. Evidence obtained by ATMI to date establishes, and ATMI hereby alleges, that the Limited Defendants have been and continue to be engaged in a pattern or practice of trade pursuant to which textile and apparel products are imported into the United States by means of false records or statements respecting their true country of origin. This pattern or practice of trade extends to numerous importations by the Limited Defendants of textile and apparel products allegedly supplied by Gaddy (HK) and Shun Tat.

69. The Limited Defendants' pattern or practice of trade also extends to their dealings with dozens of other alleged garment manufacturers in Hong Kong and Macau, not all of which have been identified by Relator. ATMI identified and its investigators visited approximately sixty-seven (67) Hong Kong and five (5) Macau

companies that were believed to be supplying garments and/or the requisite quota to facilitate the export of apparel products to the Limited Defendants through Mast (FE). However, beyond preliminary observations, ATMI was not able to make direct observations of these companies due to extremely tight security in some cases, and the lack of time and resources available to investigate every possible Hong Kong transshipper. Nevertheless, of the additional garment suppliers identified by ATMI, at least twenty (20) appeared to be engaged in the transshipment of Chinese-origin garments through Hong Kong for ultimate delivery to United States customers, including the Limited Defendants.

EVIDENCE OF FALSE RECORDS OR STATEMENTS BY DEFENDANT TARRANT (US)

70. Tarrant (US) and its affiliate Tarrant (HK) conduct significant importing operations from Hong Kong and the People's Republic of China. Tarrant (US)'s senior executives maintain strong personal relationships with suppliers and manufacturers located in Hong Kong and China. Public disclosures made by Tarrant (US) to the U.S. Securities and Exchange Commission in its 1995 Form 10-K assert that in 1995, 75.7 percent of Tarrant (US)'s imported net sales originated in Hong Kong, while 7.9 percent originated in China.

71. According to Tarrant (US)'s Form S-1 filed with the U.S. Securities and Exchange Commission in May of 1995, in order to manage this trade, Tarrant (HK) maintains an office in Hong Kong that employs approximately 150 people, many of whom have extensive knowledge

about and experience with sourcing and production in Hong Kong and China.

72. Tarrant (US) often purchases the fabric that will be used to produce garments for its customers. Upon information and belief, Tarrant (US) purchases the fabric for delivery directly to the manufacturer's factory. Generally, the factories pay Tarrant (US) for the fabric with offsets against the price of the finished goods. This arrangement places a premium on vigorous and timely quality control. Ordinarily, a buyer to whom non-conforming goods are tendered may reject the delivery and refuse to pay for the nonconforming goods. If, however, Tarrant (US) were not vigilant and failed to detect quality problems early in the manufacturing process, it would lose the value of the fabric used to produce the finished goods that failed to pass inspection at the time of delivery.

73. In its 1995 Form 10-K Report to the Securities and Exchange Commission, Tarrant (US) informed the investing public of the care it uses to maintain quality control by monitoring production activity. According to representations made in said Report, Tarrant (HK) monitors the production of apparel by its suppliers on a daily basis and provides daily status reports to its home office in Los Angeles. Both Tarrant (HK) and Tarrant (US) keep their customers apprised through daily telephone calls and reports. Tarrant (US) represents that its quality control personnel visit each factory during the manufacturing process "to inspect garments when the fabric is cut, as it is being sewn and as the garment is being finished." Form 10-K (1995), Tarrant Apparel Group, filed March 29, 1996, at 8. This quality control activity provides Tarrant

(HK) and Tarrant (US) with timely and detailed knowledge of the origin-conferring activities that take place during the manufacturing process, as well as knowledge of the attachment of false country of origin labels on finished garments.

74. As a result of competition with other retailers for reliable sources of production and available quota, coupled with the need to monitor the quality of the products produced by garment manufacturers and to safeguard the millions of yards of fabric entrusted to garment manufacturers each year, Defendant Tarrant (US) is in a position to and does monitor the origin-conferring activities of those companies that produce textile and apparel products for it. As a consequence, representations by or on behalf of Defendant Tarrant (US) to Customs with respect to the country of origin of imported textile and apparel products are based upon actual knowledge of the origin-conferring activities of their garment manufacturers, or are made in deliberate ignorance of the truth or falsity of such representations or with reckless disregard for the truth or falsity of such representations.

False Claims With Respect To Products Supplied By Ka Yick Garment Factory

75. Ka Yick Garment Factory O/B Gain Light Ltd. (hereinafter "Ka Yick") is a major supplier of apparel to Tarrant (HK). Ka Yick maintains a place of business at 1/F, Flat E, Wong King Industrial Building, 2 Tai Yau Street, San Po Kong, Kowloon, Hong Kong. Tarrant (HK) exports the apparel it procures from Ka Yick to its parent in Los Angeles, Tarrant (US), d/b/a Fashion Resource,

Inc. Tarrant (US) resells this merchandise to the Limited Defendants and other United States-based retailers that are not named as parties in this Complaint.

76. At all times material to this Complaint, Ka Yick was in receipt of and/or was in the process of fulfilling purchase orders for apparel submitted to it by Tarrant (HK) on behalf of the Limited Defendants. During April and May of 1996, Ka Yick was under contract to produce close to 100,000 pieces of apparel for Tarrant (HK), more than half of which was to bear brandnames or trademarks owned or controlled by the Limited Defendants.

77. Between February 13 and June 1, 1996, ATMI's investigators visited Ka Yick's Hong Kong facility at the Wong King Industrial Building on approximately twelve (12) occasions. At no time during these visits did ATMI's investigators observe any indication that Ka Yick was engaged in the cutting of fabric to shape or the sewing of fabric pieces for garment production. At no time did ATMI's investigators hear the sounds of sewing machines stitching garments. At no time did ATMI's investigators observe the presence of production equipment, including cutting tables or sewing machines. At no time did ATMI's investigators observe fabric being cut into pieces at Ka Yick or pieces of cut fabric being taken from Ka Yick's premises for processing elsewhere. At no time did ATMI's investigators observe evidence of Ka Yick discarding fabric scraps, remnants of thread or other residue or debris that would normally be generated by a factory that was cutting fabric or producing the quantities of apparel that Ka Yick was shipping from its factory.

78. On the basis of this evidence, ATMI hereby alleges that between February 13 and June 1, 1996, Ka Yick was not engaged at a commercially significant level in the cutting of fabric to shape, the sewing of fabric pieces, or any other operation regarded by Customs as conferring origin on apparel products.

79. On May 11, 1996, ATMI's investigators observed finished garments being delivered to Ka Yick by vehicles engaged in cross border traffic, *i.e.*, with license plates issued by both the People's Republic of China and Hong Kong. ATMI's investigators observed workers at Ka Yick repacking garments and placing them in cartons for export to the Limited Defendants. ATMI's investigators also observed workers at Ka Yick loading bolts of uncut fabric and accessories onto trucks engaged in cross-border traffic.

80. On the basis of observations made by ATMI's investigators at Ka Yick, it is evident that a person monitoring Ka Yick's operations would know or ought to know that Ka Yick was not cutting fabric or producing apparel of Hong Kong origin at its facilities in the Wong King Industrial Building.

81. Documents obtained by ATMI at Ka Yick confirm that Ka Yick routinely subcontracted for the production of apparel products for Tarrant (HK) with factories in the People's Republic of China and that such products were marked "Made in Hong Kong" prior to their importation into the United States by Tarrant (US), d/b/a Fashion Resource, Inc.

82. Tarrant (HK) submitted purchase orders to Ka Yick covering two Lane Bryant purchase orders (P.O.

518394 and P.O. 518403) for 7,812 cotton twill outer vests in assorted colors under Style No. 137418, to be shipped on May 6, 1996 on the vessel known as the President Truman. In some of the sales documents pertaining to these shipments, Ka Yick was designated the "seller," and in others, a company called Wing Tai Garment International, Ltd. (hereinafter "Wing Tai"), located at 13/F Wing Tai Centre, 12 Hing Yip Street, Kwun Tong, Kowloon, Hong Kong, was identified as the vendor. Wing Tai entered these transactions so that quota allocations owned by it could be used to support the transactions. Upon information and belief, ATMI alleges that Wing Tai was otherwise not involved in the production and sale of this merchandise.

83. As part of its overall investigation into the activities of Defendants, ATMI has been monitoring data compiled from ships' manifests (hereinafter "Ships' Manifest Data") which identify, among other things, the names of the importer, consignee and shipper and provide a description of identifying marks, and numbers associated with individual bills of lading. *See* 19 U.S.C. § 1431(c).

84. Ships' Manifest Data covering importations entering the United States between January 1995 and July 1996 show that the vests ordered by Lane Bryant arrived at Seattle, Washington on or about May 16, 1996, under bill of lading numbers OOLU95191753 and OOLU95191778. Each consignment was marked "Made in Hong Kong." This merchandise cleared Customs in Columbus, Ohio.

85. Documentary evidence obtained by ATMI discloses that the actual producer of these cotton twill outer vests was the Waterlee Garment Factory, Ltd. (hereinafter

"Waterlee"), of 6/F, T/12, Industrial Building, Lung Wu Industrial Area, Shantou, China. In particular, Waterlee shipped sixty (60) boxes of vests identified by Style No. 137418 from China to Hong Kong on May 3, 1996, and another 120 boxes of the same style vests from China to Hong Kong on May 4, 1996. Waterlee made at least one other shipment of this style to Tarrant (HK) during May 1996.

86. On May 6, 1996, Tarrant (HK) also shipped an order of twill blouses and an order of denim blouses to Tarrant (US), d/b/a Fashion Resource, Inc., aboard the President Truman. Tarrant (US) had purchased the blouses from Ka Yick on behalf of Defendant Lane Bryant, Inc. Ka Yick sold the blouses to United Garment Manufacturing Co. Ltd. (hereinafter "United Garment") of 20-24 Bute Street, I/F, Kowloon, Hong Kong, a quota holder that was designated as the exporter. Ships' Manifest Data show that United Garment shipped these blouses and that they arrived in Seattle, Washington on May 16, 1996, under bill of lading numbers OOLU95191751 and OOLU95191726. All of these blouses, numbering 18,184 pieces altogether, were marked "Made in Hong Kong," were consigned to Tarrant (US), d/b/a Fashion Resource, Inc., and were designated for eventual delivery to Defendant Lane Bryant, Inc. Because the blouses were shipped together with the 7,812 outer vests described in paragraphs 82-85, and given Ka Yick's lack of production capacity, ATMI alleges that the blouses were made by Waterlee in China, just as were the outer vests.

87. On May 11, 1996, Tarrant (US), d/b/a Fashion Resource, Inc., purchased 508 cartons of cotton woven

twill jumpers (Style No. 537781) from Ka Yick in response to Lerner's P.O. No. 19682-8. The Special Customs form associated with this transaction was signed by Ka Yick as "Seller" and indicated that the per-unit price was US$5.67. A second invoice for these garments was issued by Ka Yick to Corpmax Ltd. (hereinafter "Corpmax"), Flat B, 17/F Entertainment Building, 30 Queen's Road, Central, Hong Kong. Corpmax is a Hong Kong quota holder that was designated as the exporter of the merchandise. Upon information and belief, ATMI alleges that Corpmax's participation in this transaction was limited to providing the Hong Kong quota needed to support this transaction, but that was otherwise not involved in the production and sale of this merchandise.

88. Ka Yick issued three (3) packing lists for delivery of 21,153 garments in Style No. 537781, marked "Made in Hong Kong," for delivery to Defendant Lerner of New York, Inc. Ka Yick's Single Country Declaration form showed that it exported 21,279 jumpers of Hong Kong origin on May 12, 1996.

89. On May 30, 1996, a shipment described as containing Lerner's Style No. 537781 under P.O. 19681-9 entered the Port of Los Angeles on American President Lines under bill of lading number APLU003818611. The shipper was designated as EI Freight (H.K.) Ltd. O/B Tarrant Co. Ltd. and the consignee was designated as Fashion Resource, Inc. The shipment was marked "Made in Hong Kong."

90. Documents obtained by ATMI show that Style No. 537781 was produced for Ka Yick by Waterlee in China. ATMI discovered documents showing that Ka Yick

shipped thread to Waterlee for use in the production of Style No. 537781 and Waterlee sent production samples of this garment to Ka Yick for approval. ATMI also uncovered an outward processing agreement between Ka Yick and Waterlee that states that Waterlee only washed, riveted, labelled, ironed, and packed these garments. Based upon the complete absence of observable production activity at Ka Yick in Hong Kong, however, Ka Yick could not possibly have cut fabric and sewn 7,812 outer vests and 18,184 blouses that were shipped on May 6, in addition to the 21,279 jumpers shipped on May 12, 1996. The outward processing agreement wholly failed to reflect either the manufacturing activities actually undertaken by Waterlee or the inability of Ka Yick to accomplish the rest of the production steps in Hong Kong.

91. ATMI also uncovered documents showing that two orders were placed with Ka Yick for Style No. 537981 in connection with Lerner's P.O. 15884-0 and P.O. 15882-2. Correspondence between Ka Yick and Waterlee shows that Ka Yick supplied zippers to Waterlee for Style No. 537981 and that the garments were actually cut and sewn in China. Ships' Manifest Data show that on March 28, 1996, a shipment described as containing Lerner's Style No. 537981 under P.O. 15882-2 entered the Port of Los Angeles on American President Lines under bill of lading number APLU003389119. The shipper was designated as EI Freight (H.K.) Ltd. O/B Leighton Textiles Co. Ltd., located at 409 Lippo Sun Plaza, 28 Canton Road, Kowloon, Hong Kong, and the consignee was designated as Fashion Resource, Inc. The shipment was marked "Made in Hong Kong." Neither Ka Yick nor Waterlee was identified in the Ships' Manifest Data. Leighton Textiles

Co., Ltd. is a Hong Kong quota holder that was designated as the shipper of the merchandise. Upon information and belief, ATMI alleges that Leighton Textiles Co., Ltd.'s participation in this transaction was limited to providing the Hong Kong quota needed to support this transaction.

92. Finally, ATMI obtained evidence regarding a sale Ka Yick made to a different U.S.-based retailer purchasing through Tarrant (US), d/b/a Fashion Resource, Inc. Tarrant (HK) contracted with Ka Yick in March of 1995 for the production of 900 denim jackets, Style No. J292DT, on behalf of F.I.S., Inc., d/b/a Bum Jeans. The jackets were to be made in Hong Kong and shipped on June 20th of the same year. Ships' Manifest Data show that on July 2, 1995, a shipment described as containing Style No. J292DT (P.O. No. 00203) entered the Port of Long Beach on July 2, 1994, on American President Lines under bill of lading number APLU003738508, and was marked "Made in Hong Kong." Although Hong Kong was identified as the country of origin in Ships' Manifest Data, Waterlee produced these garments in China. A fully completed "Q.C. Inspection Report," dated June 4, 1995, concerning P.O. No. 00203 was faxed by Waterlee in China to Ka Yick in Hong Kong on that same day. This order for denim jackets was actually produced in China, not Hong Kong.

93. Additional correspondence between Ka Yick and Waterlee links Waterlee in China with orders for Style Numbers 590026, 505026, 518531, 537816, 575501, and 527815. Upon information and belief, these are all style numbers used to identify apparel products sold by the Limited Defendants.

False Claims With Respect To Products Supplied By Landale Garment Factory Ltd.

94. The Landale Garment Factory Ltd. (hereinafter "Landale") is an important supplier of apparel to Tarrant (HK). Landale maintains a place of business at 9/F, Flats 1 & 2, Perfect Industrial Building, 31 Tai Yau Street, San Po Kong, Kowloon, Hong Kong. Tarrant (HK) exports the apparel it procures from Landale to its parent in Los Angeles, Tarrant (US), d/b/a Fashion Resource, Inc. Tarrant (US) conveys this merchandise to the Limited Defendants, as well as to other United States-based retailers, including Target Stores, that are not named as parties in this Complaint.

95. At all times material to this Complaint, Landale was in receipt of and/or was in the process of fulfilling purchase orders for apparel submitted to it by Tarrant (HK) on behalf of the Limited Defendants and Target Stores. Individual documents obtained by ATMI's investigators show that Landale was under contract to Tarrant (HK) for the production of tens of thousands of pieces of apparel between January and April 1996. In April 1996 alone, Landale had purchase orders from Tarrant (HK) for not less than 48,000 pieces of apparel. All of this apparel was to bear brandnames or trademarks owned or controlled by United States-based retailers.

96. Between January 24 and June 10, 1996, ATMI's investigators visited Landale's Hong Kong facility at the Perfect Industrial Building on approximately thirty-five (35) to forty (40) occasions. At no time during these visits did ATMI's investigators see any indication that Landale

was engaged in the cutting of fabric for garment production. At no time did ATMI's investigators observe workers operating more than a few sewing machines. At no time did ATMI's investigators observe any indication that Landale was producing garments in commercially significant quantities. In fact, on many occasions, the factory was completely idle. At no time did ATMI's investigators observe fabric being cut into pieces at Landale or pieces of cut fabric being taken from Landale's premises for processing elsewhere. At no time did ATMI's investigators observe evidence of Landale discarding fabric scraps, remnants of thread or other residue or debris that would normally be generated by a factory that was producing the quantities of apparel that Landale was shipping from its facility.

97. On the basis of this evidence, ATMI hereby alleges that between January 24 and June 10, 1996, Landale was not engaged at a commercially significant level in the cutting of fabric to shape, the sewing of fabric pieces, or any other operation regarded by Customs as conferring origin on apparel products.

98. On a number of occasions between January 24 and June 10, 1996, ATMI's investigators observed finished garments being delivered to Landale by vehicles engaged in cross-border traffic, *i.e.*, with license plates issued by both the People's Republic of China and Hong Kong. On numerous occasions, ATMI's investigators observed workers at Landale folding and repacking garments and placing them in cartons for export to U.S.-based retailers. Sounds of boxes being taped shut were common throughout this period. On a number of occasions, ATMI's investigators observed workers at Landale loading bolts of

uncut fabric and accessories onto trucks engaged in cross-border traffic. Shipping documents showing the shipment of fabric by Landale to the People's Republic of China were also obtained.

99. On the basis of observations made by ATMI's investigators at Landale, it is evident that a person monitoring Landale's operations would know or ought to know that Landale was not producing apparel of Hong Kong origin at its facilities in the Perfect Industrial Building.

100. ATMI was able to identify a number of apparel shipments from Landale to Target Stores, a major customer of Tarrant (US). On January 27, 1996, ATMI's investigators observed workers at Landale working on a large quantity of garments packed in flat cartons and stacked on pallets. The cartons were marked:

> Target Stores
> P.O. No. 40349
> DPC Item No. 140-908
> Style No. 463124
> Color: Chino Tan Size 9A
> Casepack 12
> Made in Hong Kong

101. Ships' Manifest Data show that on February 10, 1996, a shipment described as containing Target Stores P.O. No. 40349 (Style No. 463124) entered the Port of Los Angeles on American President Lines under bill of lading number APLU003397066. The shipper was designated as EI Freight (H.K.) Ltd. O/B United Textiles and the consignee was designated as Fashion Resource, Inc. The shipment was marked "Made in Hong Kong."

102. On February 4, 1996, pallets being prepared for shipment were observed. ATMI estimates that there were at least 2,000 cartons in this shipment – a quantity far in excess of any observable production activity at Landale during this period. Cartons stacked on those pallets were marked:

Target Stores
P.O. No. 40348
DPC Item No. 140-903
Style No. 463124
Color: Chino Tan Size 9P
Casepack 12
Made in Hong Kong

103. Ships' Manifest Data show that on February 16, 1996, a shipment described as containing Target Stores P.O. No. 40348, Style No. 463124 (pants), entered the Port of Los Angeles on American President Lines under bill of lading number APLU003357876. The shipper was designated EI Freight (H.K.) Ltd. O/B United Textiles and the consignee was designated as Fashion Resource, Inc. The shipment was marked "Made in Hong Kong."

104. On March 2, 1996, a large shipment of cartons believed to contain blue jeans was seen being removed from Landale's premises. The following markings were displayed on the cartons:

Target Stores
P.O. No. 40415
Style No. 444153
Color: Anti Wash Size 16T(12P)(8A)
Made in Hong Kong

105. Ships' Manifest Data show that on March 15, 1996, a shipment described as containing Target Stores

P.O. No. 40415 and Style No. 444153 (jeans) entered the Port of Los Angeles on American President Lines under bill of lading number APLU003812987. The shipper was designated as United Textiles and the consignee was designated Fashion Resource, Inc. The shipment was marked, "Made in Hong Kong."

106. Between April 20 and April 25, 1996, ATMI's investigators observed stacks of used packing cartons accumulating on Landale's rear loading dock as another large shipment was prepared. Used cartons of this type are typically used to transport garments from the People's Republic of China to Hong Kong. Such garments are relabelled as the products of Hong Kong and are repacked in new cartons with overseas shipping instructions printed on the sides of the new cartons. The accumulation of used cartons has added significance with respect to Landale's shipments because, during this period, there was no observable evidence that Landale engaged in any apparel production activities at its Perfect Industrial Building facility.

107. On April 24 and 25, 1996, Landale was observed making a large shipment to Target Stores. Upon information and belief, this shipment consisted of garments that had been shipped from China in the used packing cartons observed on Landale's loading dock and that had then been repacked in new cartons. The cartons were marked for delivery as follows:

Target Stores
P.O. No. 40428
DP-CL-Item No. 017-02-0613
Style No. 441580
Color: Chambray Size 16(14)(10)(8)
Casepack-12-PCS
Made in Hong Kong

108. Ships' Manifest Data show that on May 10, 1996, shipments under five (5) separate bills of lading entered the Port of Los Angeles on American President Lines. Each of these shipments was described as containing Target Stores P.O. No. 40428 and Style No. 441580. All were marked "Made in Hong Kong." The following table shows the shippers, bill of lading numbers, and consignees shown on the manifests:

Shipper	Bill of Lading	Consignee
EI Freight (H.K.) Ltd., O/B Grand Country Trading	APLU003365655	Fashion Resource, Inc.
EI Freight (H.K.) Ltd., O/B Maple Garment Ltd.	APLU003818098	Fashion Resource, Inc.
EI Freight (H.K.) Ltd., O/B Miamiee Sportswear	APLU003818099	Fashion Resource, Inc.
EI Freight (H.K.) Ltd., O/B Tarrant Co. Ltd.	APLU003818108	Fashion Resource, Inc.
EI Freight (H.K.) Ltd., O/B Wonderfeel Garment Factory Ltd.	APLU003818097	Fashion Resource, Inc.

109. Landale also made an earlier shipment of Style No. 441580 to Target Stores on April 15, 1996. This shipment was made by sea under Tarrant (HK) purchase order number 1903069. Ships' Manifest Data show that Fashion Resources, Inc. received this shipment on April 26, 1996, under bill of lading number APLU003817957.

110. ATMI has obtained documentary proof that Landale sourced garments from factories in the People's Republic of China for shipment to Target Stores. On February 13, 1996, Landale received a seven (7) page fax from Chan Hua Garment Company Limited of Hua County, Guangdong, China, that sets forth a packing list for 111 cartons of blue jeans described as product number 444153. This number matches the style number associated with the March 2, 1996 shipment to Target Stores discussed in paragraphs 68 and 69. These garments were made in the People's Republic of China, marked "Made in Hong Kong," and loaded into an American President Lines 40-foot container bearing number APLU988516.

111. On May 6, 1996, ATMI obtained invoices directed to Landale by the Tai Kwong Transportation Company of Hong Kong. Invoice number 15522, dated February 13, 1996, described a shipment of 111 cartons of garments from Hua County (Guangdong, China) to Kowloon (Hong Kong). Upon information and belief, these garments were part of Landale's March 2, 1996 shipment to Target Stores. Ships' Manifest Data show that on March 15, 1996, a shipment matching this description arrived in Los Angeles under bill of lading number APLU003812987 marked "Made in Hong Kong."

False Claims With Respect To Products Supplied By Star River International Development Co., Ltd.

112. Star River International Development Co., Ltd. (hereinafter "Star River") is an important supplier of apparel to Tarrant (HK). Star River occupies the 17th and 18th floors at the Ban Thong Building, 15-19 Chun Pin Street, Kwai Chung, New Territories, Hong Kong. Tarrant (HK) exports the apparel it procures from Star River to its parent in Los Angeles, Tarrant (US), d/b/a Fashion Resource, Inc. Tarrant (US) conveys merchandise obtained from Star River to the Limited Defendants, as well as to other United States-based retailers that are not named as parties to this action.

113. Based upon documents obtained by ATMI, Star River is estimated to have shipped 150,000 to 200,000 garments per month during 1995 and the first half of 1996 to customers in the United States. In particular, during the months of May, June and July 1996, Star River was linked to approximately 400,000 pieces of clothing imported by Tarrant (US), d/b/a Fashion Resource, Inc. for ultimate delivery to stores owned and operated by Defendants Lerner New York, Inc. and Express Stores, Inc.

114. Between April 25 and August 13, 1996, ATMI's investigators visited Star River's Hong Kong facility at the Ban Thong Building on approximately nine (9) occasions. At no time during these visits did ATMI's investigators observe any indication that Star River was engaged in the cutting of fabric for garment production. Not more than fifteen (15) or twenty (20) sewing machines were observable at the Star River facility. With few exceptions, this production equipment was observed

to be idle and unused. At no time did ATMI's investigators observe indications that Star River was producing garments in commercially significant quantities. On most occasions, the factory was completely idle. At no time did ATMI observe fabric being cut to shape at Star River or pieces of cut fabric being taken from Star River's premises for processing elsewhere. At no time did Star River discard fabric scraps, remnants of thread or other residue or debris that would normally be generated by a factory that was cutting fabric to shape or otherwise producing the quantities of apparel that Star River was purportedly shipping from its factory.

115. On the basis of this evidence, ATMI hereby alleges that between April 25 and August 13, 1996, Star River was not engaged at a commercially significant level in the cutting of fabric to shape, the sewing of fabric pieces, or any other operation regarded by Customs as conferring origin on apparel products.

116. On a number of occasions between April 25 and August 13, 1996, ATMI's investigators either observed or obtained documents showing that finished garments were delivered to Star River by vehicles engaged in cross-border traffic, *i.e.*, with license plates issued by both the People's Republic of China and Hong Kong. On a number of occasions, ATMI's investigators observed workers at Star River folding and repacking garments and placing them in cartons for export to U.S.-based retailers. Sounds of boxes being taped shut were common throughout this period. ATMI's investigators also observed personnel at Star River loading bolts of uncut fabric and accessories onto trucks engaged in cross-border traffic.

117. ATMI has acquired documents that establish that Star River has purchased apparel accessories and/or packing material and then instructed the vendor to deliver the merchandise to an apparel factory in China. In addition, on or about October 25, 1995, Tarrant (HK) sent a fax to a textile manufacturer named Southern Dragon instructing it to deliver 66,000 yards of denim to Star River in China.

118. On August 8, 1996, Dun & Bradstreet (HK) Ltd. issued a report on the activities of Star River. That report was consistent with other evidence obtained by ATMI showing that Star River did not produce apparel in Hong Kong and that 100 percent of its production process was subcontracted to factories in the People's Republic of China.

119. An examination of Ships' Manifest Data covering importations made between August 1995 and July 1996 shows that Star River was itself identified as the shipper on twenty-seven (27) bills of lading. Tarrant (US), d/b/a Fashion Resource, Inc., was identified as the consignee in each of these transactions. In twenty-six (26) of these transactions, China was identified as the country of origin.

120. During the course of its investigation, ATMI also obtained computer-generated production information prepared by Tarrant (HK) indicating that Star River primarily supplied Tarrant (HK) with apparel alleged to be made in Hong Kong. In these entries, Star River was identified as the "Factory" while another entity was identified as the "Shipper." ATMI was able to identify Ships' Manifest Data corresponding to approximately ninety-

five (95) of the entries in said computer records. The Ships' Manifest Data did not disclose Star River's role as the "Factory," but they did identify a Hong Kong quota holder as the "Shipper" and Hong Kong as the country of origin. Each of these entries on Tarrant (HK)'s computer-generated documents is associated with a separate false claim made by Defendant Tarrant (US) that garments produced by Star River were the product of Hong Kong.

False Claims With Respect To Products Supplied By Evernew Garments Limited

121. Evernew Garments Limited (hereinafter "Evernew") is a major supplier of garments to Tarrant (HK) and its parent company, Tarrant (US), d/b/a Fashion Resource, Inc. Tarrant (US) conveys merchandise obtained from Evernew to the Limited Defendants and other U.S. apparel retailers. Evernew occupies Blocks A and B on the third floor of the Mow Hing Factory Building, 205 Wai Yip Street, Kwun Tong, Kowloon, Hong Kong.

122. Based upon documents obtained by ATMI from Tarrant (HK), Evernew was the purported manufacturer of a number of large shipments made to Tarrant (US) in mid-1996. During the months of April – September 1996, Evernew was linked to approximately 178,000 pieces of apparel scheduled to be imported into the United States by Tarrant (US), d/b/a Fashion Resource, Inc. for ultimate delivery to Defendants Express, Inc. and Lerner New York, Inc., as well as other U.S.-based retailers.

123. Evernew's facilities at the Mow Hing Factory Building in Hong Kong have insufficient production

capacity to accommodate the level of Evernew's reported sales.

124. Evernew has two affiliated garment factories in China that have ample capacity to produce apparel in the volumes needed to fill Tarrant (HK)'s orders. Together, Dongguan Kam Ip Fashion Co., Ltd. and Dongguan Kam Wing Fashion Co., Ltd. have 1,935 employees and 900 sewing machines, compared to Evernew's estimated sixty-five (65) workers and fifty (50) sewing machines located in Hong Kong. Evernew's combined monthly production capacity, based primarily upon these Chinese facilities, is approximately 28,000 garments per month.

125. An examination of Ships' Manifest Data covering all importations made between August 1995 and July 1996 shows that Evernew was identified as the shipper on a total of twenty-seven (27) bills of lading where Tarrant (US), d/b/a Fashion Resource, Inc. was also identified as the consignee. In twenty-one (21) out of these twenty-seven (27) transactions, China was identified as the country of origin.

126. During the course of its investigation, ATMI obtained two computer-generated reports prepared by Tarrant (HK) in which Evernew was identified as the "Factory" for several entries. Using purchase order numbers, ATMI was also able to identify Ships' Manifest Data corresponding to approximately twenty-one (21) entries in said computer records where Evernew was identified as the "Factory."

127. Where Evernew was identified as the "Factory" and also as the "Shipper" in Tarrant (HK)'s reports, Ships' Manifest Data disclosed Evernew's role and

showed China as the country of origin. However, where Evernew was identified as the "Factory" only and another entity was identified as the "Shipper" in Tarrant (HK)'s reports, the corresponding Ships' Manifest Data did not disclose Evernew's role. It only identified the "Shipper," or Hong Kong quota holder, and Hong Kong as the country of origin. Each of these computer entries is associated with a separate false claim made by Defendant Tarrant (US) that garments produced by Evernew were the product of Hong Kong.

False Claims With Respect To Products Supplied By Via Hong Kong Ready-To-Wear Co., Ltd.

128. Via Hong Kong Ready-To-Wear Co., Ltd. (hereinafter "Via Hong Kong") is an important supplier of apparel products to Tarrant (HK) and its parent company, Tarrant (US), d/b/a Fashion Resource, Inc. Tarrant (US) imports the merchandise into the United States on behalf of the Limited Defendants and other U.S.-based retailers not named as Defendants in this Complaint. Via Hong Kong is located at 2/F and 9/F, Suntax Tower, Wo Yee Hop Road, Kwai Chung, N.T., Hong Kong.

129. Based upon documents obtained by ATMI from Tarrant (HK), Via Hong Kong was the purported manufacturer of a number of large shipments made to Tarrant (US) in mid-1996. During the months of January – May 1996, Via Hong Kong was linked to approximately 224,000 garments imported into the United States by Tarrant (US), d/b/a Fashion Resource, Inc. Of these, 62,000 were for ultimate delivery to Defendant Lane Bryant, Inc.

130. Via Hong Kong's facilities at the Suntax Tower in Hong Kong have insufficient production capacity to accommodate the level of Via Hong Kong's reported sales to Tarrant (HK).

131. Via Hong Kong is affiliated with two garment factories in Guangdong Province in China – one in Pan Yu and one in Sha Tau Kok – that have ample capacity to produce apparel in the volumes needed to fill Tarrant (HK)'s orders. Together, these Via Hong Kong affiliates produce up to 50,000 dozen pants and 2,000 dozen shirts each month. They have 2,900 employees and 1000 sewing machines, compared to the estimated sixty to seventy (60-70) workers that ATMI investigators observed working at sewing machines at Via Hong Kong.

132. An examination of Ships' Manifest Data covering all importations made between August 1995 and July 1996 shows that Via Hong Kong was identified as the shipper on a total of forty-four (44) bills of lading. Although Tarrant (US), d/b/a Fashion Resource, Inc., was only identified as the consignee in two (2) of these bills of lading, in none of these transactions was China identified as the country of origin.

133. During the course of its investigation, ATMI obtained a computer-generated report prepared by Tarrant (HK) in which Via Hong Kong was identified as the "Factory" for several entries. By tracking the reported purchase order numbers, ATMI was also able to identify Ships' Manifest Data corresponding to approximately nineteen (19) of the entries in said computer report. Eighteen (18) of the garment shipments listed were declared to be products of Hong Kong and, in each case, Ships'

Manifest Data identified another entity as the "Shipper" and failed to disclose Via Hong Kong's role. Because the vast majority of Via Hong Kong's production capacity is located in China, each of these computer entries is associated with a separate false claim made by Defendant Tarrant (US) that garments produced by Via Hong Kong were the product of Hong Kong.

False Claims With Respect To Products Supplied By Golden Island Garment Factory

134. Golden Island Garment Factory (hereinafter "Golden Island") is a primary supplier of garments to Tarrant (HK) and its parent company, Tarrant (US), d/b/a Fashion Resource, Inc. Tarrant (US) imports the merchandise into the United States on behalf of U.S. customers including the Limited Defendants. Golden Island occupies the entire ninth floor (Flats 1-6) of the Hung Tat Industrial Building, 43 Hung To Road, Kwun Tong, Hong Kong.

135. Based upon documents obtained by ATMI from Tarrant (HK), Golden Island allegedly produced garments in significant volumes for Tarrant (US) in early 1996. In fewer than six (6) months, Tarrant (US), d/b/a Fashion Resource, Inc. procured more than 340,000 pieces of apparel from Golden Island, all of which were imported into the United States as products of Hong Kong. Of these, 70,000 pieces were for ultimate delivery to Defendant Lane Bryant, Inc.

136. Golden Island's facilities in the Hung Tat Industrial Building in Hong Kong, however, have insufficient production capacity to accommodate the level of Golden Island's reported sales.

137. Although ATMI was unable to verify whether Golden Island is affiliated with any manufacturers in China, ATMI's investigators did not observe any evidence that Golden Island had the production capacity it purported to have. ATMI's investigators did not observe the 100 workers Golden Island reportedly employs in Hong Kong. ATMI's investigators observed approximated fifty (50) employees on one visit, but on every other occasion, Golden Island's facilities were extremely quiet, lacking all sounds associated with the production of garments. Even given the fifty (50) employees present on one occasion, Golden Island did not have the production capacity to make apparel in the volumes needed to fill its orders on behalf of Tarrant (HK).

138. An examination of Ships' Manifest Data covering all importations made between August 1995 and July 1996 shows that Golden Island was not identified on any bills of lading.

139. During the course of its investigation, however, ATMI obtained a computer-generated report prepared by Tarrant (HK) in which Golden Island was identified as the "Factory" for a significant number of entries. By using purchase order numbers, ATMI was also able to identify Ships' Manifest Data corresponding to approximately forty (40) entries in said computer record. In each case, another entity was identified as the "Shipper," and the Ships' Manifest Data did not disclose Golden Island's

role in the transaction. It only identified the "Shipper," or Hong Kong quota holder, and Hong Kong as the country of origin. Each of these computer entries is associated with a separate false claim made by Defendant Tarrant (US) that garments produced by Golden Island were the product of Hong Kong.

Conclusion With Respect To The Defendant Tarrant (US)

140. On the basis of observations made by ATMI's investigators at the Hong Kong facilities of Tarrant (HK)'s various suppliers, it is evident that a person monitoring the activities of these companies would know or ought to know that these suppliers are not producing apparel of Hong Kong origin at these facilities. Moreover, Tarrant (US)'s close relationship with its suppliers in Hong Kong and China, in addition to its stated practice of monitoring every phase of production on a daily basis and of keeping its customers informed with respect to the status of their orders, makes it clear that Tarrant (US) had actual knowledge of its suppliers' practice of subcontracting production to factories in China and falsifying the country of origin on labels and documents, or it made representations with respect to country of origin with deliberate ignorance of or reckless disregard for the truth or falsity of those representations.

141. Evidence obtained by ATMI to date establishes, and ATMI hereby alleges, that Defendant Tarrant (US) has been and continues to be engaged in a pattern or practice of trade pursuant to which textile and apparel products are imported into the United States by means of

false records or statements respecting their true country of origin. This pattern or practice of trade extends to numerous other importations of textile and apparel products yet to be identified by Relator.

Allegations Applicable To
The Limited Defendants and Tarrant (US)

142. Upon each importation of textile and apparel articles, the Limited Defendants and Defendant Tarrant (US) are required to file, or cause to be filed on their behalf, with Customs certain entry documents, including but not limited to: (1) a Customs Form 7501 setting forth, among other things, the country or countries of origin of the articles to be entered into the United States, (2) one or more commercial invoices, (3) one or more declarations pursuant to 19 C. F. R. § 12.130(f), as described in paragraph 35 of this Complaint, and (4) other entry documents (hereinafter referred to collectively as "entry documents").

143. All of the aforementioned entry documents are required to contain an express certification that the statements contained therein are true and correct to the best of the declarant's information, knowledge, and belief. 19 U.S.C. § 1485 (a) (3); 19 C. F. R. § 12.130 (f).

144. The Limited Defendants and Defendant Tarrant (US) have filed or caused to be filed with Customs thousands of entry documents in which it has been claimed that imported textile and apparel articles were the product of Hong Kong or Macau, when, in fact, the articles were the product of the People's Republic of China.

145. To the extent that the entry documents filed by the Limited Defendants and Defendant Tarrant (US) in connection with the transactions identified in this complaint represented that the imported textile or apparel articles were the products of Hong Kong or contained fabric that was cut to shape in Hong Kong, such entry documents were false. Said false entry documents were used to enter or introduce textile and apparel products into the commerce of the United States that were not entitled to admission and that were not marked with the true country of origin.

146. Defendants knew that such entry documents were false, acted in deliberate ignorance of the truth or falsity of the claims made in said entry documents, or acted with reckless disregard for the truth or falsity of the claims made in said entry documents.

COUNT ONE

(Concealment of Obligation to Forfeit Merchandise or its Value to the United States Pursuant to 18 U.S.C. § 545)

147. Paragraphs 1 through 146 are realleged and incorporated herein by reference.

148. Defendants have imported or caused to be imported into the United States thousands of shipments of textile and apparel products.

149. Some or all of these textile and apparel products were marked, labelled and/or declared to be the product of Hong Kong or Macau, when in fact these

articles were the product of the People's Republic of China.

150. Importing or causing to be imported products into the United States that are marked, labelled and/or declared to be the product of Hong Kong or Macau, when, in fact, the articles are the product of the People's Republic of China, is contrary to law.

151. Whenever a person knowingly or fraudulently imports or brings into the United States any merchandise contrary to law, or receives, conceals, buys, sells, or in any manner facilitates the transportation, concealment, or sale of such merchandise after importation, knowing the same to have been imported or brought into the United States contrary to law, the merchandise in question or the value thereof shall be forfeited to the United States. 18 U.S.C. § 545.

152. Defendants have knowingly or fraudulently imported or caused to be imported thousands of shipments of textile and apparel products that were marked, labelled, and/or declared to be the product of Hong Kong or Macau, when, in fact, the articles were the product of The People's Republic of China, contrary to law.

153. The Limited Defendants and Defendant Tarrant (US) have bought, sold or facilitated the transportation of textile and apparel products that have been imported into the United States contrary to law.

154. Defendants are obligated to forfeit to the United States all textile and apparel products, or the value thereof, imported into the United States contrary to law. 18 U.S.C. § 545.

155. The actions of said Defendants in making or causing to be made or used false records or statements to Customs has resulted in concealment of the fact that the subject merchandise failed to comply with applicable laws and regulations governing both admission into the United States and country of origin marking, thereby allowing said Defendants to conceal and avoid their obligation to forfeit the merchandise or its value to the United States, as required by 18 U.S.C. § 545, all in violation of the False Claims Act, 31 U.S.C. § 3729(a)(7).

COUNT TWO

(Concealment of Obligation to Pay Civil Penalty Equal to the Value of the Merchandise Pursuant to 19 U.S.C. § 1595a(b))

156. Paragraphs 1 through 146 are realleged and incorporated herein by reference.

157. The Defendants directed, assisted, or were otherwise concerned with the importation, bringing in, unloading, landing or removal, concealing or harboring, or subsequent transportation of textile and apparel products that were being or have been introduced into the domestic commerce of the United States.

158. Some or all of these textile and apparel products were marked, labelled and/or declared to be the product of Hong Kong or Macau, when, in fact, these articles were the product of the People's Republic of China.

159. Importing or causing the importation of products into the United States that are marked, labelled and/

or declared to be the product of Hong Kong or Macau, when, in fact, the articles are the product of the People's Republic of China, is contrary to law.

160. Every person who directs, assists financially or otherwise, or is in any way concerned in the importation or bringing in, unloading, landing, or removal, concealing or harboring, or subsequent transportation of any article which is being or has been introduced into the United States contrary to law, is liable for a civil penalty in the amount of the domestic value of the article. 19 U.S.C. § 1595a(b).

161. Defendants directed, assisted or were otherwise concerned with the importation, bringing in, unloading, landing or removal, concealing or harboring, or subsequent transportation of textile and apparel products that were being or have been introduced into the United States contrary to law.

162. Defendants have become liable and are liable for and obligated to pay to the United States a civil penalty in the amount of the domestic value of the textile and apparel articles imported by them into the United States contrary to law. 19 U.S.C. § 1595a(b).

163. The actions of said Defendants in making or causing to be made or used false records or statements to Customs has resulted in concealment of the fact that the subject merchandise failed to comply with applicable laws and regulations governing both admission into the United States and country of origin marking, thereby allowing said Defendants to conceal and avoid their obligation to pay to the United States a civil penalty in an amount equal to the domestic value of the merchandise,

as required by 19 U.S.C. 1595a(b), all in violation of the False Claims Act, 31 U.S.C. 3729(a)(7) .

COUNT THREE

(Concealment of Obligation to Pay Civil Penalty Pursuant to 19 U.S.C. § 1592)

164. Paragraphs 1 through 146 are realleged and incorporated herein by reference.

165. Defendants entered, introduced, or attempted to introduce, or aided or abetted other persons who entered, introduced, or attempted to introduce textile and apparel products into the domestic commerce of the United States.

166. Some or all of these textile and apparel products were marked, labelled and/or declared to be the product of Hong Kong or Macau, when, if fact, these articles were the product of the People's Republic of China.

167. Without regard to whether the United States is or may be deprived of all or a portion of any lawful duty thereby, no person, by fraud, gross negligence, or negligence may enter, introduce, or attempt to enter or introduce any merchandise into the commerce of the United States by means of any document or electronically transmitted data or information, written or oral statement or act which is material and false, or any omission which is material, or may aid or abet any other person in committing such violations. 19 U.S.C. § 1592(a)(1). Such violations are punishable by a civil penalty in an amount not

to exceed the domestic value of the merchandise. *Id.* § 1592(c).

168. Entering, introducing, or attempting to enter or introduce, or aiding or abetting any person that enters, introduces, or attempts to enter or introduce textile and apparel products that are marked, labelled and/or declared to be the product of Hong Kong or Macau, when in fact these articles are the product of the People's Republic of China, is contrary to law.

169. Defendants entered, introduced, or attempted to enter or introduce, or aided or abetted persons that entered, introduced, or attempted to enter or introduce textile and apparel products by means of material and false oral or written statements or omissions in violation of 19 U.S.C. § 1592(a).

170. Defendants have become liable and are liable for and obligated to pay to the United States a civil penalty not to exceed the domestic value of the articles imported in violation of 19 U.S.C. § 1592(a). 19 U.S.C. § 1592(c).

171. The Limited Defendants and Defendant Tarrant (US) have filed or caused to be filed with Customs thousands of entry documents in which it has been claimed that imported textile and apparel articles were the product of Hong Kong or Macau, when, in fact, the articles were the product of the People's Republic of China. Said declarations were both material and false and were used to enter or introduce inadmissible and falsely marked merchandise into the commerce of the United States in violation of 19 U.S.C. § 1592.

172. The actions of said Defendants in making or causing to be made or used false records or statements to Customs has resulted in concealment of the fact that the subject merchandise failed to comply with applicable laws and regulations governing both admission into the United States and country of origin marking, thereby allowing Defendants to conceal and avoid their obligation to pay to the United States a civil penalty in an amount not to exceed the domestic value of the merchandise, as required by 19 U.S.C. § 1592, all in violation of the False Claims Act, 31 U.S.C. § 3729(a)(7).

COUNT FOUR

(Concealment of Obligation to Pay Liquidated Damages)

173. Paragraphs 1 through 146 are realleged and incorporated herein by reference.

174. Defendants, as importers of record of textile and apparel products, are required to file with Customs a bond to permit importation and release of the subject merchandise and to secure the Customs transactions. 19 U.S.C. § 1623 and 19 C.F.R. Part 113.

175. Defendants filed with Customs single entry or continuous basic importation and entry bonds for all entries of textile and apparel products made by said Defendants.

176. The terms of the respective bond(s) require Defendants, as principals, to agree to: (1) pay all duties, taxes and charges, (2) make or complete an entry to enable Customs to determine whether the merchandise

may be released, and (3) make or complete an entry to enable Customs to determine whether the applicable requirements of law and regulation are met. 19 C.F.R. § 113.62(a) and (b).

177. In addition, Customs' regulations provide that a condition of every basic importation and entry bond is an agreement by the principal to redeliver timely, on demand by Customs, any merchandise that has been conditionally released if the merchandise fails to comply with the laws or regulations governing admission into the United States or if it must be marked with the proper country of origin. 19 C.F.R. § 113.62(d).

178. If the principal defaults on this agreement, or breaches the bond, the principal and surety, jointly and severally, agree to pay liquidated damages equal to the lawful entered value of the merchandise as defined by 19 U.S.C. § 1401a. 19 C.F.R. §§ 113.62(k)(1) and 141.113(a) and (b).

179. Defendants breached the terms of their respective bond(s) by failing to provide Customs with complete and accurate entry information to enable Customs to determine whether the merchandise may be released, or whether applicable requirements of law or regulation, including laws and regulations governing the entry of merchandise subject to lawful quotas, were met.

180. Defendants also breached the terms of their respective bond(s) by failing to pay additional marking duties due to the United States pursuant to 19 C.F.R. § 1304(f). *See* Count Five, below.

181. Defendants are liable for and obligated to pay to the United States liquidated damages equal to the lawful entered value of the merchandise as defined by 19 U.S.C. § 1401a. 19 C.F.R. §§ 113.62(k) and 141.113(a) and (b).

182. The actions of said Defendants in making or causing to be made or used false records or statements to Customs has resulted in concealment of the fact that the subject merchandise failed to comply with applicable laws and regulations governing both admission into the United States and country of origin marking, thereby resulting in Defendants breaching their bond(s), and allowing Defendants to avoid their obligation to pay to the United States liquidated damages equal to the lawful entered value of the imported merchandise, as required by 19 C.F.R. §§ 141.113(a) and 141.113(b), all in violation of the False Claims Act, 31 U.S.C. § 3729(a)(7).

COUNT FIVE

(Concealment of Obligation to Pay Marking Duties)

183. Paragraphs 1-146 are realleged and incorporated herein by reference.

184. Goods having false country of origin markings that enter the United States after evading destruction, re-exportation, or remarking under Customs custody are subject to an additional ten percent (10%) *ad valorem* marking duty which "shall not be . . . avoidable for any cause." 19 U.S.C. § 1304(f).

185. Defendants imported textile and apparel products that were marked made in Hong Kong or Macau,

when, in fact, these products were produced in the People's Republic of China. Such products were not destroyed, re-exported, or remarked under Customs custody.

186. Defendants have become liable and are liable for and obligated to pay the United States a ten percent (10%) *ad valorem* additional marking duty for all improperly marked textile and apparel products imported by Defendants into the United States. 19 U.S.C. § 1304 and 19 U.S.C. § 1592(d).

187. The Limited Defendants and Defendant Tarrant (US) have filed or caused to be filed with Customs thousands of entry documents in which it has been claimed that imported textile and apparel articles were the products of Hong Kong or Macau when, in fact, the articles were the product of the People's Republic of China. Said entry documents constituted false records or statements that masked the real country of origin of the falsely marked imported articles and permitted Defendants to conceal their obligation to pay a ten percent (10%) *ad valorem* marking duty on each of said articles as required by 19 U.S.C. § 1304(f) and 19 U.S.C. § 1592(d), all in violation of the False Claims Act, 31 U.S.C. § 3729(a)(7).

COUNT SIX

(Concealment of Obligation to Pay Civil Penalties for Violation of the Federal Trade Commission Act)

188. Paragraphs 1-146 are realleged and incorporated herein by reference.

189. The importation into the United States of any textile fiber product which is misbranded is unlawful and constitutes an unfair method of competition and an unfair and deceptive act or practice in commerce under the Textile Fiber Products Identification Act, 15 U.S.C. § 70a(a) and the Federal Trade Commission Act, 15 U.S.C. § 45(m).

190. An imported textile fiber product is misbranded if it is not labelled with the name of the country where it is processed or manufactured. *Id.* § 70b(b)(4).

191. At all times material to this Complaint, the Limited Defendants and Defendant Tarrant (US) imported or caused to be imported into the United States textile fiber products that were misbranded within the meaning of the Textile Fiber Products Identification Act, as amended, 15 U.S.C. § 70b(b)(4).

192. Said Defendants' importation of misbranded textile fiber products constitutes an unfair method of competition and an unfair and deceptive act or practice in commerce under the Federal Trade Commission Act for which said Defendants are subject to the imposition of civil penalties of up to $US10,000 per violation. 15 U.S.C. §§ 45(m) and 70e.

193. Defendants have filed or caused to be filed thousands of entry documents in which it has been claimed falsely that certain textile fiber products were the products of Hong Kong or Macau when, in fact, the articles were the products of the People's Republic of China. The actions of said Defendants in making or causing to be made or used false records or statements to Customs has permitted Defendants to conceal the fact

that the imported articles were misbranded and avoid their obligation to pay civil penalties for importing misbranded textile fiber products as required by 15 U.S.C. §§ 45(m) and 70e, all in violation of the False Claims Act, 31 U.S.C. § 3729(a)(7).

COUNT SEVEN

(Liability of The Limited, Inc. for Certain Acts of the Tarrant Apparel Group)

194. Paragraphs 1-35 and 70-193 are realleged and incorporated herein by reference.

195. The Limited, Inc. and Limited Direct Associates, L.P., exercise significant control over the commercial activities of Defendant Tarrant (US). Transactions involving The Limited, Inc. and its affiliated companies represent a significant percentage of Tarrant (US)'s overall business.

196. Tarrant (US)'s sales to subsidiaries of The Limited, Inc. (*i.e.*, Express, Inc. Lerner New York, Inc. and The Limited London-Paris-New York, Inc.) represented 63.6, 56.8, and 48.6 percent of Tarrant (US)'s total sales for 1993, 1994, and 1995, respectively. During the first quarter of 1996, sales to divisions of The Limited, Inc. rose to 62.8 percent of Tarrant (US)'s total sales.

197. On May 4, 1995, Tarrant (US) filed a Form S-1 Registration Statement with the Securities and Exchange Commission in which it announced to the investing public that:

> [a]s a result of the importance of The Limited to the operation of the Company, The Limited and

> its divisions have the ability to exert significant influence over the Company's business decisions.

Form S-1, Tarrant Apparel Group, filed May 4, 1995, at 6.

198. The control exercised by The Limited, Inc. over Tarrant (US) and its operations extends to participation in integrated teams of design, merchandising, and support personnel from both companies that focus on designing and producing merchandise. These teams are responsible for monitoring production and delivering finished products. The first formal teams were organized in 1992 for The Limited London-Paris-New York, Inc. and Lerner New York, Inc. Later, a separate team was formed for Lane Bryant, Inc.

199. All or substantially all of the merchandise imported by Tarrant (US) for The Limited, Inc. and its subsidiaries clears Customs at the Columbus, Ohio port of entry where it is delivered to central distribution facilities operated by the Limited Defendants.

200. All of said imported merchandise is marked or labelled at the time it is produced with brandnames and/or trademarks owned or controlled by the Limited Defendants. The styles, colors, patterns, fabrics, sizes, and quantities of this merchandise are all controlled by the Limited Defendants and are designed to fit within the Limited Defendants' seasonal merchandising plans and to complement other apparel purchases by the Limited Defendants.

201. Tarrant (US) has no legal right to import and distribute for its own account merchandise with

brandnames and trademarks owned or controlled by the Limited Defendants.

202. Limited Direct Associates, L.P. (hereinafter "LDA") is a limited partnership. Limited Direct, Inc. is the general partner of LDA. All of the shares of Limited Direct, Inc. are owned by the Defendant The Limited, Inc.

203. On or about July 24, 1995, 2,000,000 additional shares in Tarrant (US) were offered for sale to the public in an initial public offering. Concurrently with the July 24, 1995 closing of Tarrant (US)'s initial public offering, and at the request of The Limited, Inc., Defendants Guez and Kay granted to LDA a four year option to purchase from them approximately ten percent (10%) of the total shares outstanding of Tarrant (US) at a price of $7.20 per share.

204. The granting of said stock option at the request of The Limited, Inc. is evidence of the degree of control that The Limited, Inc. exercises over Tarrant (US) and Defendants Guez and Kay. The existence of this option is in itself an instrumentality through which control may be exercised.

205. The control exercised by the Limited Defendants over the commercial activities of Defendant Tarrant (US), coupled with the close collaboration between said Defendants in the design, merchandising, production, and importation of apparel from Hong Kong, Macau, and the People's Republic of China, including the filing of false records or statements with Customs designed to permit Tarrant (US) to evade quota restrictions and conceal the obligation to transfer money or property to the U.S. government as alleged in Counts One through Six

hereof, constitutes a joint enterprise for which the Limited Defendants are jointly and severally liable with Tarrant (US) under the False Claims Act.

COUNT EIGHT

(Personal Liability of Defendants Guez and Kay)

206. Paragraphs 1-35 and 70-193 are realleged and incorporated herein by reference.

207. At all times material to this Complaint, Defendants Gerard Guez and Todd Kay held a controlling interest in Defendant Tarrant (US). Prior to the July 24, 1995 initial public offering of stock in Defendant Tarrant (US), Defendants Guez and Todd owned 100 percent of Tarrant (US)'s stock. Following the initial public offering, Defendants Guez and Kay together held 61.6 percent of Tarrant (US)'s stock.

208. In their positions as majority shareholders and chief executive and chief operating officers of Tarrant (US), respectively, Defendants Guez and Kay exercise absolute control over the day-to-day business activities of Tarrant (US) and Tarrant (HK).

209. Defendants Guez and Kay are active in the day-to-day interactions with Defendant Tarrant (US)'s suppliers in Hong Kong and the People's Republic of China. In its Form S-1 Registration Statement filed with the Securities and Exchange Commission on May 4, 1995, Tarrant (US) made the following representation:

> The Company's senior management has historically had and continues to have strong relationships with suppliers and manufacturers located in Hong Kong and China.

Form S-1, Tarrant Apparel Group, filed May 4, 1995, at 25. Several times a year, members of Tarrant (US)'s senior management visit and inspect the facilities and operations of the company's international suppliers and manufacturers.

210. As a result of their substantial holdings of the shares of Tarrant (US), their personal relationships with Tarrant (US)'s suppliers in Hong Kong, and the People's Republic of China, their regular visits to Tarrant (US)'s key suppliers in Hong Kong, Macau, and the People's Republic of China, and their personal involvement in the day-to-day management of Tarrant (US) and Tarrant (HK), Defendants Guez and Kay are personally liable for the acts of Tarrant (US) that are the subject of this Complaint.

PRAYER FOR RELIEF

WHEREFORE, Relator prays for a final judgment in favor of ATMI and the United States of America and against Defendants:

(1) Declaring that Defendants have violated the False Claims Act;

(2) Requiring Defendants to render an accounting of all sums owed to the United States on account of importations made by them during the ten (10) year period immediately preceding the filing of this Complaint;

(3) Ordering the Defendants, jointly and severally, to pay the United States three times the amount of the value of all textile and apparel products entered into the commerce of the United States by means of Defendants' false records or statements, in that Defendants concealed and avoided their obligation to pay said sums for civil forfeitures and/or penalties, as required by 18 U.S.C. § 545, in violation of 31 U.S.C. § 3729(a)(7);

(4) Ordering the Defendants, jointly and severally, to pay the United States three times the amount of the domestic value of all textile and apparel products entered into the commerce of the United States by means of Defendants' false records or statements, in that Defendants concealed and avoided their obligation to pay said sums for penalties for aiding unlawful importation pursuant to 19 U.S.C. § 1595a(b), in violation of 31 U.S.C. § 3729(a)(7);

(5) Ordering the Defendants, jointly and severally, to pay the United States three times the amount of the domestic value of all textile and apparel products entered into the commerce of the United States by means of Defendants' false records or statements, in that Defendants concealed and avoided their obligation to pay said sums for civil penalties for fraudulent, grossly negligent, or negligent importation of merchandise pursuant to 19 U.S.C. § 1592, in violation of 31 U.S.C. § 3729(a)(7);

(6) Ordering the Defendants, jointly and severally, to pay the United States three times the amount of liquidated damages owed under 19 C.F.R. §§ 113.62(k) and 141.113(a) and (b) in that Defendants concealed and avoided their obligation to pay said sum for failure to

redeliver inadmissible and mismarked merchandise, in violation of 31 U.S.C. § 3729(a)(7);

(7) Ordering the Defendants, jointly and severally, to pay the United States three times the amount of marking duties owed under 19 U.S.C. § 1304(f), in that Defendants concealed and avoided their obligation to pay said sum for importing merchandise bearing false country of origin markings in violation of 31 U.S.C. § 3729(a)(7);

(8) Ordering Defendants, jointly and severally, to pay the United States three times the amount of civil penalties arising under the Textile Fiber Products Identification Act and the Federal Trade Commission Act, 15 U.S.C. §§ 45(m) and 70a, in that Defendants concealed and avoided their obligation to pay said sums for having imported misbranded textile fiber products in violation of 31 U.S.C. § 3729(a)(7);

(9) Imposing a penalty against Defendants, jointly and severally, of $10,000 for each false record or statement found to have been made by Defendants, as provided for in 31 U.S.C. § 3729(a);

(10) Requiring Defendants jointly and severally, to pay pre-judgment and post-judgment interest at applicable statutory rates;

(11) Declaring that the Limited Defendants are liable jointly and severally with the Defendant Tarrant (US) for damages and penalties imposed upon the Defendant Tarrant (US) arising out of the importations made by Defendant Tarrant (US) on behalf of the Limited Defendants.

(12) Declaring that the Defendants Guez and Key [sic] are personally liable, jointly and severally, for the damages and penalties owed by Defendant Tarrant (US);

(13) Requiring Defendants, jointly and severally, to pay Relator a sum equal to all reasonable attorneys fees, costs, and expenses incurred by Relator in connection with this proceeding, as provided for in 31 U.S.C. § 3730(d)(1);

(14) Requiring the United States to pay Relator an award out of the damages and penalties collected from Defendants, as provided for in 31 U.S.C. § 3730(d)(1)-(3); and

(15) For such other relief as the Court may deem just and proper.

DEMAND FOR JURY TRIAL

Pursuant to Federal Rule of Civil Procedure 38(b) and Rule 3.4.10.1 of the Rules of the United States District Court for the Central District of California, Relator demands trial by jury of any and all issues triable of right by a jury.

DATED: September 25, 1996

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